

Contract Law

NEIL ANDREWS
University of Cambridge



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Contract Law

This textbook takes a fresh approach to contract law; as a first edition it reflects the subject in the 21st century more accurately than other texts. Comprehensive and scholarly, it maps the curriculum perfectly but detailed references and further reading sections encourage students to explore the subject further. Understanding is paramount and chapter introductions clearly guide students through the material. The textbook takes an innovative approach to case law: breaking down and discussing individual elements of a case and selecting short key extracts, it gives students the tools to read cases independently and with confidence. An examination of the historical and theoretical foundations of the subject and a concluding chapter tracking emerging fields ensure the broadest possible perspective. Discussion of key recent cases such as *Durham Tees Valley Airport* (2010) and *Chartbrook* (2009) make this important new text a must for contract law students.

Neil Andrews is an experienced contract law teacher and scholar. A Fellow of Clare College Cambridge, he has published widely: his publications include *English Civil Procedure* (2003) and *The Modern Civil Process* (2008).

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For
Liz, Samuel, Hannah and Ruby

and
In memory of

Kurt Lipstein
1909–2006
Professor of Comparative Law, University of Cambridge
Fellow of Clare College
Bencher of Middle Temple

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Contents

<i>Preface</i>	<i>page</i> ix
<i>Table of cases</i>	xi
<i>Table of statutes</i>	xlvi
<i>Table of statutory instruments</i>	xlvi
Part I Introduction	1
1 Main features of contract law	3
Part II Formation	17
2 The pre-contractual phase	19
3 Offer and acceptance	37
4 Certainty	89
Part III Consideration and intent to create legal relations	115
5 Consideration and estoppel	117
6 Intent to create legal relations	171
Part IV Third parties and assignment	185
7 Third parties	187
8 Assignment	225
Part V Vitiating elements	233
9 Misrepresentation	235
10 Mistake	275
11 Duress, undue influence and unconscionability	307
Part VI Terms and interpretation	343
12 Terms in general	345
13 Implied terms	353
14 Interpretation and rectification of written contracts	379
15 Exclusion clauses	419

Part VII Breakdown and liability	443
16 Frustration	445
17 Breach and performance	475
Part VIII Remedies for breach	517
18 Judicial remedies for breach of contract	519
19 Consensual remedies for breach of contract: liquidated damages and deposits	599
Part IX Illegality and public policy	619
20 The illegality doctrine	621
Part X The future	647
21 International and European 'soft law' codes: lessons for English law?	649
<i>Appendix: A who's who of contract law</i>	673
<i>Bibliography</i>	697
<i>Index</i>	724

Preface

I hope that this guide to the English law of contract will be of use and interest to both students and lawyers in practice.

I have provided the reader with introductory summaries to each topic. Chapter 14 reflects the very considerable importance of interpretation of written contracts, which practitioners are not slow to name as the most important aspect of contract law. In addition, I decided to include chapters on illegality and assignment, and a concluding chapter on three topical matters: ‘good faith’, European ‘soft law’ codes, and the (perennial, but perhaps pressing) question of case law technique versus codification. This is an ‘adult book’: ‘minors’, since small, are confined to paragraph 1.09.

By the use of varying fonts, the reader can locate quickly discussion of greater detail, including substantial portions of quoted text, and take appropriate action, perhaps sometimes evasive. Paragraph numbering has facilitated cross-referencing, which is particularly important in this cohesive subject where doctrines are closely connected or overlap. In each chapter there is a short list of further selected reading. At the end of the book there is a copious general bibliography. There is also in the appendix to this book a set of ‘cameo’ biographies of the leading writers and judges (dead or retired) who have shaped this subject.

I have been lucky to have taught this subject in Cambridge since 1983. I am grateful to many generations of law students, from whom I have learned a great deal. Contract law students in the early 1980s were wrestling with judgments of the recently retired Lord Denning and of Lord Diplock, who gave his last judgment in 1985. Current students are similarly engaged with the bold judgments of the recently retired Lord Hoffmann, notably, *Attorney-General for Belize v. Belize Telecom Ltd* (2009, PC), discussed at 13.15; *Chartbrook Ltd v. Persimmon Homes Ltd* (2009, HL), on which see 14.14, 14.22, 14.35, 14.46; and *Transfield Shipping Inc. v. Mercator* (*‘The Achilles’*) (2008, HL), on which see 18.43, 18.45 ff. During the long interval we have witnessed the brilliant lucidity of Lords Bingham, Browne-Wilkinson, Goff, Hobhouse, Millett, Mustill, Nicholls and Steyn (to confine the list to retired members of the House of Lords), and the proliferation of new textbooks and other works on contract law. During these last three decades there has also been an avalanche of scholarship in restitution or unjust enrichment, and judicial absorption of this learning.

I pay filial tribute to those who taught me various parts of the English law of obligations at Brasenose College, Oxford, 1977–80 (BA) and 1981–2 (BCL): Hugh Collins

(now Professor at the London School of Economics, and my college tutor in contract law at Oxford), John Davies (a Herculean teacher), Professor Bernard Rudden (sometime Professor of Comparative Law), the late Professor Peter Birks (Regius Professor of Civil Law, Oxford) and Professor Barry Nicholas (sometime Professor of Comparative Law, later Principal of Brasenose College).

I have also learned a great deal from my teaching colleagues in the University of Cambridge who have taught contract law or cognate subjects, and I pay respectful homage to their example. In recent years I have also benefited from discussion on 'vitiating factors' with Gareth Spark, PhD, my former research pupil (now University of East Anglia). Lord Grabiner of Aldwych, QC (Head of Chambers, One Essex Court; formerly Chairman of the Court of Governors, London School of Economics, 1998–2007) has also generously encouraged me. None of those mentioned in this preface has been asked to comment on this text, for which I am, therefore, wholly responsible and culpable.

My thanks are due to the members of Cambridge University Press who have assisted in this publication, and especially to Sinéad Moloney who kindly invited me to publish with this distinguished press.

I am grateful to my wife, Elizabeth Deyong, and our children, Samuel, Hannah and Ruby. Their good humour has enabled me to keep the law fully at arm's length outside normal business hours. I have been remarkably blessed.

Table of cases

4 Eng Ltd v. Harper [2008] EWHC 915 (Ch); [2009] 3 WLR 892, 73, 255, 550, 553
A Roberts & Co. Ltd v. Leicestershire CC [1961] CH 555, 413
A to Z Bazaars (Pty) Ltd v. Minister of Agriculture (1974) (4) SA 392 (c), 56
Abrahams v. Herbert Reiach Ltd [1922] 1 KB 477, CA, 94, 543
Actionstrength Ltd v. International Glass Engineering In.Gl.En SpA [2003] 2 AC 541, HL, 122, 123, 130
Adam Opel GmbH v. Mitras Automotive UL Ltd [2008] EWHC 3205 (QB); [2008] Bus LR D55, 320
Adam Phones Ltd v. Gideon Goldschmidt, 9 July 1999, 530
Addis v. Gramophone Co. Ltd [1909] AC 488, HL, 484, 541, 551
Agip SpA v. Navigazione Alta Italia SpA ('The Nai Genova') [1984] 1 Lloyd's Rep 353, CA, 413, 414
Aiton Australia Pty Ltd v. Transfield Pty Ltd [1999] NSWSC 996, 29
Ajayi v. Briscoe [1964] 1 WLR 1326, PC, 155, 158
Akerblom v. Price (1881) 7 QBD 129, CA, 340
Alan v. El Nasr [1972] 2 QB 189, CA, 152–3
Albert v. Motor Insurers Bureau [1972] AC 301, HL, 179
Albon v. Naza Motor Trading Sdn Bhd [2007] EWCA Civ 1124, 100
Alec Lobb (Garages) Ltd v. Total Oil GB Ltd [1983] 1 WLR 87, 334, 335–6, 341
'The Alex' [1989] 1 Lloyd's Rep 138, 319
Alexander v. Rayson [1936] 1 KB 169, CA, 634
Alf Vaughan & Co. v. Royscot Trust plc [1999] 1 All ER (Comm) 856, 319
Alfred McAlpine Capital Projects v. Tilebox Ltd [2005] EWHC (TCC) 281; [2005] BLR 271, 602, 603, 605
Alfred McAlpine Construction Ltd v. Panatown [2001] 1 AC 518, HL, 193, 199, 200, 202, 204, 545, 548
Alfred Toepfer International GmbH v. Itex Itagrani Export SA [1993] 1 Lloyd's Rep 360, 486
'The Alhazero' [1977] AC 774, HL, 202, 204
Ali v. Christian Salvesen [1997] 1 All ER 721, CA, 370, 372
Ali Shipping Corporation v. Shipyard Trogir [1999] 1 WLR 314, CA, 358
Allcard v. Skinner (1887) 36 Ch D 1455, CA, 323, 325, 326, 337
Allcard v. Skinner [1896] 2 Ch 369, 291

- Allianz SpA v. West Tankers (C-185/07) [2009] 1 AC 1138; [2009] 1 Lloyd's Rep 413, 350
- Allied Maples Group v. Simmons & Simmons [1995] 1 WLR 1602, CA, 73, 550
- Allied Marine Transport Ltd v. Vale do Rio Doce Navegação SA ('The Leonidas D') [1985] 1 WLR 925, CA, 47-8
- Alpenstow Ltd v. Regalian Properties Ltd [1985] 1 WLR 721, 174
- Amalgamated Investment & Property Co. Ltd v. John Walker & Sons Ltd [1977] 1 WLR 164, CA, 450, 452
- Amalgamated Investment & Property Co. Ltd v. Texas Commerce International Bank Ltd [1981] 1 All ER 923 [1982] QB 84, CA, 161, 165, 167, 387-8, 400
- Amalgamated Society of Railway Servants v. Osborne [1910] AC 87, HL, 635
- Anangel Atlas Compania Naviera SA v. Ishikawajima Harima Heavy Industries Co. Ltd (No. 2) [1990] 2 Lloyd's Rep 526, 146
- Anderton v. Clwyd CC (No. 2) [2002] 1 WLR 997, CA, 287
- Andrews v. Hopkinson [1957] 1 QB 229, 252
- Andrews v. Mockford [1896] 1 QB 372, CA, 241
- Anglia Television Ltd v. Reed [1972] 1 QB 60, CA, 544
- Anglo Petroleum Ltd v. TFB (Mortgages) Ltd EWCA Civ 456; [2007] BCC 407, 640
- Ansprop Trading Ltd v. Harris Distribution Ltd [1997] 1 WLR 1025, 192
- Antaios Cia Naviera SA v. Salen Rederierna AB [1985] AC 191, HL, 388, 390, 498
- Antons Trawling Co. Ltd v. Smith [2002] NZCA 331; [2003] 2 NZLR 23, 119, 145
- Aoterroa International Scancarriers [1985] 1 NZLR 513, PC, 97
- Archbolds (Freightage) Ltd v. S Spanglett Ltd [1961] 1 QB 374, CA, 627, 639
- Arcos v. Ronaasen [1933] AC 470, HL, 503-4, 662
- Argo Fund Ltd v. Essar Steel Ltd [2005] EWHC 600, 138
- Aribisala v. St James Homes etc. (No. 1) [2007] EWHC 1694 (Ch), 614-15
- Ariston SRL v. Charly Records (Court of Appeal 13 March 1990), 606
- Arkin v. Borchard Lines Ltd [2005] EWCA Civ 655; [2005] 1 WLR 3055, 635
- Ashmore, Benson, Pease & Co. Ltd v. AV Dawson Ltd [1973] 1 WLR 828, CA, 622
- Ashville Investments Ltd v. Elmer Contractors Ltd [1989] QB 488, CA, 417
- ASM Shipping Ltd of India v. TTME Ltd of England ('The Amer Energy') [2009] 1 Lloyd's Rep 293, 566
- Assicurazioni Generali SpA v. Arab Insurance Group (BSC) [2002] EWCA Civ 1642; [2003] 1 All ER (Comm) 140, 246, 247, 272, 383
- Associated British Ports v. Ferryways NV [2009] EWCA Civ 189; [2009] 1 Lloyd's Rep 595, 180
- Associated Japanese Bank Ltd v. Crédit du Nord SA [1989] 1 WLR 255, 282, 288
- Associated Provincial Picture Houses v. Wednesbury Corporation [1948] 1 KB 223, CA, 29, 369
- AT&T Corporation v. Saudi Cable Co. [2000] 2 Lloyd's Rep 127, 27
- Atlantic Lines & Navigation Co. Inc. v. Hallam ('The Lucy') [1983] 1 Lloyd's Rep 188, 263
- Atlas Express Ltd v. Kafco (Importers and Distributors) Ltd [1989] QB 833, 319-20

- Attica Sea Carriers Corporation v. Ferrostaal Poseidon Bulk Reederei GmbH ('The Puerto Buitrago') [1976] 1 Lloyd's Rep 250, CA, 527, 528
- Attorney-General v. Blake [2001] 1 AC 268, HL, 11, 520–1, 541, 588, 589, 592, 594, 603, 670
- Attorney-General for Belize v. Belize Telecom Ltd [2009] UKPC 10; [2009] 2 All ER 1127; [2009] BCC 433, 354–5, 366, 367, 371–3
- Attorney-General of Hong Kong v. Humphreys Estates (Queens Gardens) Ltd [1987] 1 AC 114, PC, 174, 347
- Attwood v. Lamont [1920] 3 KB 571, CA, 642
- Avon Insurance plc v. Swire Fraser Ltd [2000] 1 All ER (Comm) 573; [2000] Lloyd's Rep IR 535, 235, 241, 257
- Avraamides v. Colwill [2006] EWCA Civ 1533; [2007] BLR 76, 207
- Awwad v. Geraghty [2001] QB 570, CA, 636, 644
- AXA Reinsurance (UK) v. Field [1996] 1 WLR 1026, HL, 383
- B & S Contracts & Design Ltd v. Victor Green Publications Ltd [1984] ICR 419, CA, 314, 319
- Bacardi-Martini Beverages Ltd v. Thomas Hardy Packaging Ltd [2002] EWCA Civ 549, CA, 431, 434
- Bacon v. Cooper (Metals) Ltd [1982] 1 All ER 397, 581
- Baird Textile Holdings Ltd v. Marks & Spencer plc [2001] EWCA Civ 274; [2002] 1 All ER (Comm) 737, 89, 91, 93, 97, 159, 173, 180, 181, 525
- Baker v. Black Sea & Baltic General Insurance Co. Ltd [1998] 1 WLR 974, HL, 373
- Balfour v. Balfour [1919] 2 KB 571, CA, 172, 175
- Balfour Beatty v. Docklands Light Railway (1996) 78 BLR 49, CA, 376
- Balfour Beatty v. Scottish Power 1994 SLT 807; *The Times*, 23 March 1994, 557, 569
- Baltic Shipping Co. v. Dillon ('The Mikhail Lermontov') (1993) 176 CLR 344, 586
- Banco de Portugal v. Waterlow & Sons Ltd [1932] AC 452, HL, 578
- Bank Line v. Arthur Capel & Co. [1919] AC 435, HL, 446, 451
- Bank of Australasia v. Palmer [1897] AC 540, PC, 406
- Bank of New Zealand v. Finivan [1991] 1 NZLR 178, 181
- Bank of Nova Scotia v. Hellenic Mutual War Risks ('The Good Luck') [1989] 3 All ER 628, CA, 353, 507
- Bankers Insurance Company Ltd v. South [2003] EWHC 380 (QB), 441
- Banks v. Cox [2002] EWHC (Ch) 2166, 243, 254, 256
- Bannerman v. White [1861] 10 CB (NS) 844, 249
- Banque Bruxelles Lambert v. Australian National Industries Ltd (1989) 21 NSWLR 502, 181
- Banque Bruxelles Lambert SA v. Eagle Star Insurance Co. Ltd (the 'SAAMCO' case) [1995] QB 375, 559, 572
- Banque Bruxelles Lambert SA v. Eagle Star Insurance Co. Ltd (the 'SAAMCO' case) [1997] AC 191, HL, 570
- Banque Keyser Ullman SA v. Skandia (UK) Insurance Co. Ltd [1980] 1 QB 665, CA, 272
- Barber v. NWS Bank plc [1996] 1 WLR 641, CA, 492, 586

- Barclays Bank v. O'Brien [1994] 1 AC 180, HL, 325, 326, 331, 332, 333
- Barclays Bank plc v. Fairclough Building [1995] QB 214, CA, 583
- Barry v. Croskey (1861) 2 J & H 1, 241
- Barry v. Davies (trading as Heathcote Ball & Co.) [2000] 1 WLR 1962, CA, 70, 77, 129
- Barton v. Armstrong [1976] AC 104, PC, 248, 314, 315
- BCC Worldwide Ltd v. Bee Load Ltd [2007] EWHC 134 (Comm), 33
- BCCI v. Aboody [1990] 1 QB 923, 321
- BCCI v. Ali [2000] 3 All ER 51, CA, 86
- BCCI v. Ali [2002] 1 AC 251, HL, 6, 12, 85, 271, 293, 665
- BCCI v. Ali [2003] 3 All ER 51, CA, 79
- BCCI SA (in liquidation) v. Ali (No. 2) [2002] EWCA Civ 82; [2002] 3 All ER 750; [2002] ICR 1258; [2002] IRLR 460, 360, 540
- Bea Hotels NV v. Bellway LLC [2007] EWHC 1363 (Comm), 349
- Beale v. Taylor [1967] 1 WLR 1193, CA, 248
- Beer v. Bowden [1981] 1 WLR 522, CA, 102
- Behnke v. Bede Shipping Co. Ltd [1927] 1 KB 649, 531
- Bell v. Lever Bros Ltd [1932] AC 161, HL, 84, 85, 271, 276, 279, 280–1, 282, 283, 284–5, 288, 289, 290, 665
- Bell v. Tuohy [2002] EWCA Civ 423; [2002] 3 All ER 975, CA, 530
- Belvoir Finance Co. v. Stapleton [1971] 1 QB 210, CA, 641
- Belzadi v. Shaftesbury Hotels Ltd [1992] Ch 1, CA, 499
- Benedetti v. Sawiris [2009] EWHC 1330, 588
- Beresford v. Royal Insurance Co. Ltd [1938] AC 586, HL, 626, 627
- Berg v. Sadler & Moore [1937] 2 KB 158, CA, 643
- Berkeley Community Villages Ltd v. Pullen [2007] EWHC 1330 (Ch); [2007] 3 EGLR 101; [2007] 24 EG 169 (CS); [2007] NPC 71, 24, 33, 377, 485, 661
- Bernuth Lines Ltd v. High Seas Shipping Ltd ('The Eastern Navigator') [2005] EWHC 3020 (Comm.); [2006] 1 Lloyd's Rep 537, 51
- Berry v. British Transport Commission [1962] 1 QB 306, CA, 543
- Beswick v. Beswick [1968] AC 58, HL, 192, 199, 209, 210, 214, 524, 532, 533
- Bhimji v. Chatwani [1991] 1 WLR 989, 530
- Bidaisee v. Sampath (1995) 46 WIR 461, PC, 615
- Bigos v. Boustead [1951] 1 All ER 92, 645
- Birkett v. Acorn Business Machines Ltd [1999] 2 All ER 429, 643
- Birmingham & District Land Co. v. London & NW Railway Co. (1888) 40 Ch 268, CA, 154
- Birmingham City v. Forde [2009] EWHC 12 (QB); [2010] 1 All ER 802, 131, 328
- Bishops Wholesale Newsagency Ltd v. Surridge Dawson Ltd [2009] EWHC 2578 (Ch), 402
- Bisset v. Wilkinson [1927] AC 177, PC, 240
- Black v. Wilcox (1976) 70 DLR (2nd) 192, 335
- Black v. Yates [1992] 1 QB 526, 168
- Blackburn Bobbin v. TW Allen [1918] 2 KB 467, CA, 458, 459
- Blackpool and Fylde Aero Club v. Blackpool BC [1990] 1 WLR 1195, CA, 72, 74, 663

- Blomley v. Ryan (1956) 99 CLR 362, 335
 BMS Computer Solutions Inc. v. AB Agri Ltd [2010] EWHC 464 (Ch), 472
 Bolton v. Mahadeva [1972] 1 WLR 1009, CA, 514, 515
 Bolton MBC v. Torkington [2004] Ch 66, CA, 8, 121
 Boone v. Eyre (1779) 1 Hy Bl 273n, 514
 ‘The Borag’ [1981] 1 All ER 856, CA, 579
 Boulton v. Jones (1857) 27 LJ Ex 117, 297, 304
 Boustany v. Piggott (1995) 69 P & CR 298, 335, 336
 Bowerman v. ABTA LTD [1996] CLC 451, 67, 172
 Bowmakers Ltd v. Barnet Instruments Ltd [1945] KB 65, CA, 641
 Boyo v. Lambeth LBC [1994] ICR 727, 507
 BP Exploration Co. (Libya) Ltd v. Hunt (No. 2) [1979] 1 WLR 783, 467, 470, 514
 BP Refinery (Westernport) Pty Ltd v. Shire of Hastings (1978) 52 ALJR 20, PC, 365
 Brace v. Calder [1895] 2 KB 253, CA, 575
 Braithwaite v. Foreign Hardwood Co. [1985] 2 KB 543, CA, 508
 Bremer Vulcan v. South India Shipping Corporation Ltd [1981] AC 909, HL, 349
 Brennan v. Bolt Burdon [2003] EWCA Civ 1017; [2005] QB 303, 238, 276, 281, 283, 286, 287, 293, 412, 644
 Bridge v. Campbell Discount [1962] AC 600, HL, 603, 604, 606
 Bridgewater v. Griffiths [2000] 1 WLR 524, 166
 Brikom Investments v. Carr [1979] 1 QB 467, CA, 251
 ‘The Brimnes’ [1975] QB 929, CA, 52, 63
 Brinkibon v. Stahag Stahl [1983] 2 AC 34, HL, 45
 Bristol Airport plc v. Powdrill [1990] Ch 744, CA, 531
 British & Benningtons v. North West Cachart Co. [1923] AC 48, HL, 508
 British & Commonwealth Holdings plc v. Quadrex Holdings Inc. [1989] QB 842, 499
 British Crane Hire Corporation Ltd v. Ipswich Plant Hire Ltd [1975] QB 303, CA, 374, 424
 British Movietonews Ltd v. London District Cinemas [1952] AC 166, HL, 445, 456
 British Racing Drivers Club v. Hextall Erskine & Co. [1996] BCC 727, 543
 British Steel Corporation v. Cleveland Bridge and Engineering Company [1984] 1 All ER 504, 21–3, 89, 107, 108, 175–7, 587
 British Westinghouse Electric Co. Ltd v. Underground Electric Railways [1912] AC 673, HL, 573, 579
 Britvic Soft Drinks Ltd v. Messer Ltd [2002] 1 Lloyd’s Rep 20; [2002] 3 All ER (Comm) 321, 431, 434
 Brown v. Gould [1972], 94
 Brown v. KMR Services Ltd [1995] 4 All ER 598, CA, 524, 556, 569, 571
 Brown v. Raphael [1958] Ch 636, CA, 239
 Brown v. Rice [2007] EWHC 625 (Ch), 124
 Brunsdon v. Humphrey (1884) 14 QBD 141, CA, 542
 BS & N Ltd (BVI) v. Micado Shipping Ltd (Malta) (‘The Seaflower’) [2001] 1 Lloyd’s Rep 341, 491
 Buehler AG v. Chronos Richardson Ltd [1998] 2 All ER 960, CA, 168

- Bunge Corporation v. Tradax Export SA [1981] 1 WLR 711, HL, 491, 492, 493, 499
- Burmah Oil Co. v. Bank of England, *The Times*, 4 July 1981, Ch, 336
- Burrell Enterprises, Re [1973] 1 WLR 19, CA, 530
- Business Environment Bow Lane Ltd v. Deanwater Estates Ltd [2007] EWCA Civ 622; [2007] L & TR 26, 174, 249, 250, 251
- Butler Machine Tool Co. Ltd v. Ex-Cell-O Corporation (England) Ltd [1979] 1 WLR 401, CA, 59, 60, 424
- Butlin's Settlement, Re [1976] 1 Ch 351, 408
- Byrne v. Van Tienhoven (1880) 5 CPD 344, 52
- C & P Haulage v. Middleton [1983] 1 WLR 1461, CA, 545
- C Czarnikow Ltd v. Koufos ('The Heron II') [1969] 1 AC 358, HL, 556, 560, 561, 658
- Cable & Wireless plc v. IBM UK [2002] 2 All ER (Comm) 1041, 29, 32, 34, 348, 595–6, 661
- Cain v. Clarica Life Insurance (2005) 263 DLR (4th) 368, 335, 336
- Callisher v. Bischoffsheim (1870) LR 5 QB 449, CA, 131
- Calvert v. William Hill Credit Ltd [2008] EWCA Civ 1427; [2009] Ch 330, 12, 273, 283, 330, 413, 539, 571, 586, 588, 590, 591, 661
- Campbell v. Frisbee [2002] EWCA Civ 1374; [2003] ICR 141, 511
- Canada Steamships Lines Ltd v. R. [1952] AC 192, PC, 425
- Cantor Fitzgerald International v. Horkulak [2004] EWCA Civ 1287; [2005] ICR 402, 94, 543
- Caparo Industries plc v. Dickman [1990] 2 AC 605, HL, 128
- Car & Universal Finance Co. v. Caldwell [1965] 1 QB 525, CA, 261, 301
- Carcia v. National Australia Bank Ltd (1998) 194 CLR 395, 331
- Carillion Construction Ltd v. Felix UK Ltd [2001] BLR 1, 319
- Carleton v. Strutt & Parker [2008] EWHC 424; 118 Con LR 68; [2008] 5 Costs LR 736; (2008) 105(15) LSG 24; (2008) 158 NLJ 480, 35
- Carlill v. Carbolic Smoke Ball Co. [1893] QB 256, CA, 41, 65, 67, 173, 669
- Carmichael v. National Power plc [1999] UKHL 47; [1999] 1 WLR 2042, 384, 387
- Carr-Glynn v. Frearson [1998] 4 All ER 225, CA, 196
- Carter v. Boehm (1766) 3 Burr 1905, 662
- Casey's Patents, Re [1892] 1 Ch 104, CA, 129, 132–3
- Catlin Estates Ltd v. Carter Jonas [2005] EWHC 2315 (TCC); [2006] PNLR 273, 204
- CCC Films v. Impact Quadrant Ltd [1985] QB 16, 545
- CDV Software Entertainment AG v. Gamecock Media Europe Ltd [2009] EWHC 2965 (Ch), 402
- Cellulose Acetate Silk Co. Ltd v. Widnes Foundry (1925) Ltd [1933] AC 20, HL, 603, 609, 610
- Central London Property Trust Ltd v. High Trees House Ltd [1947] 1 KB 130, 119, 154–5, 156, 157, 162
- Centrovincial Estates plc v. Merchant Investors Assurance Co. Ltd [1983] Com LR 158, 80, 294
- Chai Sau Yin v. Liew Kwee Sam [1962] AC 304, PC, 628

- Champion Investments Ltd v. Ahmed [2004] EWHC 1956 (QB), 283, 293
 Chandelor v. Lopes (1603) Cro Jac 4, 249
 Chandler v. Webster [1904] 1 KB 493, CA, 467
 Chapelton v. Barry UDC [1940] 1 KB 532, CA, 424
 Chapman v. Honig [1963] 2 QB 502, CA, 376
 Chappell & Co. Ltd v. Nestle [1960] AC 87, HL, 130
 Charge Card Services Ltd, Re [1989] Ch 497, CA, 356
 Charles Rickards Ltd v. Oppenheim [1950] 1 KB 616, CA, 152, 153
 Charnock v. Liverpool Corporation [1968] 1 WLR 1498, 252
 Chartbrook Ltd v. Persimmon Homes Ltd [2009] UKHL 38; [2009] AC 1101, 380, 394, 395–6, 397–8, 399, 401, 402–4, 409, 411, 414–15
 Charter Reinsurance Co. Ltd v. Fagan [1997] AC 313, HL, 392, 393, 494, 495, 498
 Chief Constable of the Greater Manchester Police v. Wigan AFC [2008] EWCA Civ 1449; [2009] 1 WLR 1580, 134
 Chillingworth v. Esche [1924] 1 Ch 97, CA, 174
 Chwee Kin Keong v. Digilandmall.com Pte Ltd [2005] 2 SLR 502, 81, 289
 CIBC Mortgages plc v. Pitt [1994] 1 AC 200, HL, 322, 325, 326, 331, 332, 333
 Cines Bes Filmclik ve Yapincilik AS v. United International Pictures [2003] EWCA Civ 1669, 606
 Citibank NA v. Brown Shipley [1991] 2 All ER 690, 298
 City & Westminster Properties (1934) Ltd v. Mudd [1959] Ch 129, 249, 251
 Clarion Ltd v. National Provident Institution [2000] 1 WLR 1888, 279
 Clarke v. Dunraven ('The Satanita') [1897] AC 59, HL, 42, 43
 Clay v. Yates (1856) 1 H & N 73, 627
 Clea Shipping Corporation v. Bulk Oil International ('The Alaskan Trader') [1984] 1 All ER 129, 524, 527
 Cleaver v. Mutual Reserve Fund Life Association [1892] 1 QB 147, 198
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Table of statutes

Alcoholic Liquor Duties Act 1979, 41

Animals Act 1971, 585

Arbitration Act 1996, 101, 667

s. 1, 349

s. 3, 349

s. 5, 636

s. 6(1), 100

s. 7, 101, 264

s. 48(5), 417

s. 49(3), 597

s. 82(1), 349

ss. 89–91, 428

Bills of Exchange Act 1882, 667

Building Societies Act 1962, 628

Carriage of Goods by Sea Act 1992, 206

Children and Young Persons Act 1933, 41

Companies Act 1985, 206

Consumer Credit Act 1974, 341

Consumer Protection Act 1987, 585

Contempt of Court Act 1981, 530

Contracts (Rights of Third Parties) Act 1999, 4, 5, 9, 150, 187, 188, 197–8, 206, 213, 215, 231, 666

s. 1(3), 207

s. 1(6), 208, 218

s. 2(1), 211–12

s. 2(2), 212–13

s. 2(3), 213

s. 3(2), 210

s. 4, 213–14

s. 5, 214–15

s. 6(5), 218

s. 7(1), 214

s. 7(3), 215

- s. 8(1), 215–16
- s. 10, 207
- Courts and Legal Services Act 1990, 123, 635
- Disability Discrimination Act 2005, 41
- Explosives Act 1875, 41
- Financial Services and Markets Act 2000, 628
- Firearms Act 1968, 41
- Fireworks Act 2003, 41
- Gambling Act 2005, 622, 629–30
- Indian Contract Act 1872, 56, 667–8
- Insolvency Act 1986, 131
- Late Payment of Commercial Debts (Interest) Act 1998, 596
- Law of Property Act 1925
 - s. 49(2), 5, 614, 615
 - s. 136(1), 227
 - s. 196, 166
- Law of Property (Miscellaneous Provisions) Act 1989, 8, 27, 123
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 - s. 1(3), 469, 470, 471, 514
 - s. 1(5), 471
- Licensing Act 2006, 41
- Limitation Act 1980, 5
 - s. 5, 5, 11
 - s. 8, 5, 11
- Marine Insurance Act 1906, 667
- Matrimonial Causes Act 1973
 - s. 25, 633
- Merchant Shipping Act 1995, 340
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 - s. 2(1), 235, 243, 244, 253, 256–60, 265, 271, 279, 410, 583
 - s. 2(2), 262, 263, 662
 - s. 3, 265–70, 420, 426–7
- National Assistance Act 1948, 135
- Offensive Weapons Act 1996, 41
- Partnership Act 1890, 667
- Police Act 1996, 134
- Restriction of Offensive Weapons Act 1959, 41

Sale of Goods Act 1979, 5, 354, 356, 504, 651, 667

s. 3, 6

s. 6, 280, 282

s. 8, 89, 98, 101

ss. 12–15, 86

ss. 13–15, 502

s. 13(1), 248, 503

s. 14(3), 577

s. 15(2), 83

s. 15A, 476, 502, 575, 662

ss. 50(3) and 51(3), 575

s. 53(3), 553

Senior Courts Act 1981, 123, 538, 596

Statute of Frauds Act 1677, 130

Supply of Goods and Services Act 1982, 5, 356

Supreme Court of Judicature Acts 1873 and 1875, 12, 127

Trade Union and Labour Relations (Consolidation) Act 1992, 174

Trading with the Enemy Act 1939, 622, 634

Unfair Contract Terms Act 1977, 5, 62, 63, 340, 341, 426, 427–37, 609, 666

s. 2(1), 420, 429

s. 3, 420, 429, 436

s. 6(1), 420, 430

s. 6(2), 420, 430

s. 6(3), 430

s. 12(1)(a) and (b), 427

s. 13(1), 427, 428

s. 14, 427

Unsolicited Goods and Services Act 1971, 47

Violent Crime Reduction Act 2006, 41

Table of statutory instruments

Conditional Fee Agreements Order 1998 (SI 1998 No. 1860), 123
Conditional Fee Agreements (Revocation) Regulations 2005 (SI 2005 No. 2305), 123
Consumer Protection (Distance Selling) Regulations 2000 (SI 2000 No. 2334), 47
Disability Discrimination Act (Amendment) Regulations 2003 (SI 2003 No. 1673), 41
Electronic Commerce (EC Directive) Regulations 2002 (SI 2002 No. 2013), 47
Poisons Rules 1982 (SI 1982 No. 218), 41
Unfair Terms in Consumer Contracts Regulations 1999 (SI 1999 No. 2083), 5, 341, 425,
437–42, 600, 604, 609, 610, 662

I

Introduction

Chapter contents

1. Characteristics of English contract law *para. 1.01*
2. Freedom of contract *para. 1.08*
3. The objective principle *para. 1.10*
4. Overview of contractual doctrines *para. 1.11*
5. Contract and tort law *para. 1.22*
6. Contract and restitution or unjust enrichment *para. 1.24*
7. Common law and equity *para. 1.25*
8. Good faith *para. 1.27*
9. European Union law *para. 1.28*
10. Transnational contract law *para. 1.29*
11. Bibliography *para. 1.30*
12. A who's who of contract law *para. 1.31*

1

Main features of contract law

1. CHARACTERISTICS OF ENGLISH CONTRACT LAW

- 1.01 English contract law is organised into topics, as set out in the chapter headings of this work. These form the ‘general part’ of the subject.¹ English contract law assumed its current shape in the nineteenth century, although there was much doctrinal development or legislative change during the twentieth century (remarks to this effect by Brian Simpson,² Patrick Atiyah,³ David Ibbetson,⁴ Michael Lobban,⁵ and Steve Hedley).⁶ As Hedley explains:⁷

Speaking in broad terms, the Victorians invented the idea that the law will enforce contracts as such. They were given a law of contracts, but turned it into a law of contract, with general principles applicable to all agreements. The responsibility for this development is largely that of Leake [1st edition, 1867], Pollock [1st edition, 1876] and Anson [1st edition, 1879], who each produced major textbooks expounding a law of contract and not merely collecting together rules on different types of contracts. The subject matter of contract was overwhelmingly business and consumer transactions; the general principles of contract were thus largely designed for commercial work.

1 Cf Roman law, which comprises a system of particular contracts: B. Nicholas, *An Introduction to Roman Law* (Oxford, 1962), 165 ff.

2 A. W. B. Simpson, (1975) 91 LQR 247, at 250–7, notes especially the influence of textbook writers: see next note.

3 P. S. Atiyah, *Essays on Contract* (Oxford, 1986), 16 ff: ‘[I]t was the nineteenth century which very largely saw the supersession of the importance of special kinds of contracts by the general principles of contract. It was, of course, an Age of Principles.’ P. S. Atiyah, *The Rise and Fall of Freedom of Contract* (Oxford, 1979), 681 ff, notes the importance of the textbooks by Leake (1867), Pollock (1875) and Anson (1879), especially the latter two; Atiyah’s remarkable historical *magnum opus* surveys the entire intellectual and economic scene; another attractive survey is W. Swain, ‘The Classical Model of Contract: The Product of a Revolution in Legal Thought?’ (2010) 30 LS 513.

4 D. Ibbetson, *A Historical Introduction to the Law of Obligations* (Oxford, 1999), chapters 5, 11, 12 and 13.

5 M. Lobban, in W. Cornish, J. S. Anderson, R. Cocks, M. Lobban, P. Polden and K. Smith, *The Oxford History of the Laws of England*, vol. XII, 1820–1914: *Private Law* (Oxford, 2010), 295 ff.

6 (1985) 5 OJLS 391, 402.

7 *Ibid.*

In modern times, Parliament⁸ and judges⁹ have consistently assumed the existence of a coherent body of general rules applicable to all types of contracts. Other legal systems organise the subject in a similar fashion, distilling general rules and doctrines of ‘contract law’, and distinguishing this unifying or shared body of law from the particular features of specific contracts, such as sale of goods, insurance, hire, employment, etc.

- 1.02 During the last twenty years, much collaborative energy has been spent identifying principles of contract acceptable to legal systems in general, whether common law, civilian or other. In fact, there are three ‘soft law’ codes (see 21.01 ff for details): (1) the global ‘commercial’ contract code, UNIDROIT’s *Principles of International Commercial Contracts* (2004);¹⁰ (2) ‘PECL’, the *Principles of European Contract Law*, by the Commission for European Contract Law;¹¹ and (3) ‘CFR’, the *Common Frame of Reference*.¹² None of these is binding, either in England and Wales or elsewhere. But, on many topics in this book, reference will be made to common features or differences between English law and these ‘soft law’ codes (for example, there are over 170 references to ‘UNIDROIT’ in these pages).
- 1.03 The ‘general part’¹³ of English contract law is a combination of rules and principles. ‘Rules’ tend to be quite specific; ‘principles’ rather more general. Principles (properly so-called) tend to be fundamental standards underpinning many rules. We will consider two such principles below: the principle of ‘freedom of contract’ (at 1.08) and ‘the objective principle’ (at 1.10).¹⁴
- 1.04 Rules can sometimes be subject to exceptions, and such exceptions can proliferate (for example, the cluster of exceptions to the rule in *Woodar’s* case, 17.23 ff). The fact that the courts have recognised a network of exceptions often reveals that the major rule is itself unsatisfactory.

8 E.g. the Misrepresentation Act 1967 (9.14) applies to all contracts and to deeds; the Contracts (Rights of Third Parties) Act 1999 applies to all contracts and deeds, except five specific categories (7.35).

9 E.g. Roskill LJ’s judgment in *‘The Hansa Nord’* [1976] QB 44, 71, CA (general concept of ‘innominate term’ applicable to sale of goods transactions).

10 2nd edn, Rome, 2004. M. J. Bonell of the University of Rome, ‘La Sapienza’, has had a remarkable influence upon this influential work; see also his Bonell, ‘Do We Need a Global Commercial Code?’ (2000–3) 5 *Uniform Law Review / Revue de droit uniforme* 469–81; M. J. Bonell (ed.), *The UNIDROIT Principles in Practice: Case Law and Bibliography on the UNIDROIT Principles of International Commercial Contracts* (2nd edn, Ardsley, NY, 2006); S. Vogenauer and J. Kleinheisterkamp (eds.), *Commentary on the UNIDROIT Principles of International Commercial Contracts* (Oxford, 2009), 21.02.

11 O. Lando and H. Beale (eds.), *Principles of European Contract Law* (The Hague, 2000), 21.02.

12 *Principles, Definitions and Model Rules of European Private Law Draft Common Frame of Reference*, ed. Christian von Bar and Eric Clive (6 vols., Oxford University Press/Sellier, 2010), prepared by the ‘Study Group on a European Civil Code’ and the ‘Research Group on EC Private Law (Acquis Group)’; project (3) is in part a revision of project (2).

13 On the ‘general part’, see S. A. Smith, ‘The Limits of Contract’, in J. W. Neyers, R. Bronaugh and S. G. A. Pitel (eds.), *Exploring Contract Law* (Oxford, 2009), 1–24; and, for a civilian perspective, see H. Dedek, ‘Border Control: Some Comparative Remarks on the Cartography of Obligations’, in J. W. Neyers, R. Bronaugh and S. G. A. Pitel (eds.), *Exploring Contract Law* (Oxford, 2009), 2 ff, especially at 36 ff.

14 For a summary of deeper values within contract law, see Martijn Hesselink, ‘European Contract Law? A Matter of Consumer Protection, Citizenship, or Justice?’, in *Liber Amicorum Guido Alpa: National Private Law Systems* (London, 2007), 500, 516–20.

- 1.05 It must be admitted, however, that it is hard to maintain a clean distinction between rules and principles because of the tendency of judges to refer to some rules or doctrines as 'principles'. Consider the following examples of this usage. First, in *Dunlop Pneumatic Tyre Co. Ltd v. Selfridge & Co. Ltd* (1915),¹⁵ Viscount Haldane LC said:

[C]ertain principles are fundamental. One is that only a person who is a party to a contract can sue on it. Our law knows nothing of a *jus quaesitum tertio* [a right of action exercisable by a third party] arising by way of contract. Such a right may be conferred by way of property, as, for example, under a trust, but it cannot be conferred on a stranger to a contract as a right to enforce the contract in *personam* [as a matter of obligation, as distinct from a right of property]. A second principle is that if a person with whom a contract not under seal has been made is to be able to enforce it consideration must have been given by him to the promisor or to some other person at the promisor's request.

These so-called 'principles' are, respectively, the common law rule that a third party cannot sue upon a contract (this remains the starting point, but statute has now enabled third parties to acquire rights of action, 17.34) and the common law rule that only a person who has provided consideration (an element of bargain) to support a promise can sue the defendant for breach of contract (in the absence of a formal contract known as a 'deed') (on deeds, 1.14 and 5.03; generally on the consideration doctrine, see chapter 5).

- 1.06 English contract law is predominantly a case law subject. There are few statutes governing the general part of contract law, although the topics of exclusion clauses and unfair terms in consumer contracts are now dominated by legislation. The main statutes affecting general contract law are: the Law of Property Act 1925 (notably section 49(2), concerning deposits, 19.32); the Law Reform (Frustrated Contracts) Act 1943; the Law Reform (Contributory Negligence) Act 1945; the Misrepresentation Act 1967; the Unfair Contract Terms Act 1977; the Sale of Goods Act 1979; the Supply of Goods and Services Act 1982; the Contracts (Rights of Third Parties) Act 1999; and the Unfair Terms in Consumer Contracts Regulations 1999. There is also the Limitation Act 1980: the limitation periods (see further 1.23) applicable to contractual actions are: six years for ordinary ('simple')¹⁶ contracts and twelve years for deeds; for the latter, 5.03.¹⁷ The possibility of codification of contract law is discussed at 21.25.¹⁸
- 1.07 English contract law has a reputation for precision and stability (although it has been fairly stated that finding this 'precise' statement often involves expensive legal advice, in order that decades or centuries of case law can be combed).¹⁹ Foreign businesses often

¹⁵ [1915] AC 847, 853, HL.

¹⁶ Section 5 of the Limitation Act 1980.

¹⁷ Section 8 of the Limitation Act 1980 refers to actions on 'specialties', for example, a deed.

¹⁸ Noting especially M. Arden, 'Time for an English Commercial Code?' [1997] CLJ 516; R. Goode, 'Removing the Obstacles to Commercial Law Reform' (2007) 123 LQR 602–17.

¹⁹ R. Goode, 'Removing the Obstacles to Commercial Law Reform' (2007) 123 LQR 602–17.

choose English law to govern their transactions by use of 'choice of law' clauses: 12.05. Such 'cross-border' transactions occur when one or both parties are resident or situated outside England.

2. FREEDOM OF CONTRACT²⁰

- 1.08 This principle, recognised both in English law and in other legal traditions,²¹ permits parties to conclude agreements on a wide range of matters, and on such terms as they wish. The principle embraces the following liberties. First, parties have a general freedom to enter into transactions which are intended (explicitly or otherwise) to create legal obligations. This freedom includes the power to formulate individual terms within such a transaction, or to acquiesce in 'default' terms 'implied' by statute or common law. Secondly, parties to a transaction can stipulate that it will not be legally binding, 6.05. Thirdly, freedom to contract includes the liberty to compromise a legal dispute, or to waive legal liability. But a contract of compromise must be very clearly worded if it is to extend one party's prospective liability towards the other, that is, liability which has not yet arisen but which might arise in the future if there were to be a change in the law.²²
- 1.09 Exercise of these interrelated freedoms is subject to the overarching limitations of (1) public policy (5.73 and chapter 20); (2) the parties' inability to exclude liability for fraud at common law: 15.04; (3) statutory regulation of adhesion clauses (15.08, 15.33); and (4) personal capacity. As regards personal capacity, for persons under eighteen (so-called 'minors'), for reasons of space the law on this topic can only be sketched in this note;²³ as for mental capacity, it should be noted that, if a party's insanity is not known to the

20 *Chitty on Contracts* (30th edn, London, 2008), 1-011 ff; P. S. Atiyah, *The Rise and Fall of Freedom of Contract* (Oxford, 1979); *Atiyah's Introduction to the Law of Contract* (6th edn, Oxford, 2006); R. Brownsword, *Contract Law: Themes for the Twenty-First Century* (2nd edn, Oxford, 2006), chapter 2; H. G. Collins, *The Law of Contract* (4th edn, Cambridge, 2003); C. Fried, *Contract as Promise: A Theory of Contractual Obligation* (Cambridge, MA, 1981); J. Gordley, *The Philosophical Origins of Modern Contract Doctrine* (Oxford, 1991); D. Kimel, *From Promise to Contract* (Oxford, 2005), chapter 5; D. Ibbetson, *A Historical Introduction to the Law of Obligations* (Oxford, 1999), chapters 7, 11, 12 and 13; S. A. Smith, *Contract Theory* (Oxford, 2004); and M. J. Trebilcock, *The Limits of Freedom of Contract* (Cambridge, MA, 1997).

21 M. J. Bonell (ed.), *The UNIDROIT Principles in Practice: Case Law and Bibliography on the UNIDROIT Principles of International Commercial Contracts* (2nd edn, Ardsley, NY, 2006), 69; S. Vogenauer and J. Kleinheisterkamp (eds.), *Commentary on the UNIDROIT Principles of International Commercial Contracts* (Oxford, 2009), 118.

22 *BCCI v. Ali* [2001] UKHL 8; [2002] 1 AC 251, at [19], [21], [35] and [86]; cf the dissent at [73] by Lord Hoffmann; N. Andrews, *English Civil Procedure* (Oxford, 2003), 23.65 to 23.77; see also *Satyam Computer Services Ltd v. Upaid Systems Ltd* [2008] EWCA Civ 487; [2008] 2 All ER (Comm) 465, at [84].

23 *Chitty on Contracts* (30th edn, London, 2008), 8-002 ff (see also S. Hedley, [2004] CLJ 435, 440-2); (1) a minor is liable for 'necessaries' purchased: section 3 of the Sale of Goods Act 1979; *Nash v. Inman* [1908] 2 KB 1, CA; 'necessaries' can include certain services (*Chitty on Contracts* (30th edn, London, 2008), 8-013); (2) a minor is bound by a contract of employment or apprenticeship as long as it is on the whole beneficial to him; but this does not extend to a contract to promote the prospects of a talented footballer: *Proform Sports Management Ltd v. Proactive Sports Management Ltd* [2006] EWHC 2903 (Ch); [2007] 1 All ER 542 (the 'Wayne Rooney' case); (3) contracts for the sale or purchase of land, or the grant or acquisition of a lease, or for the onerous acquisition of shares, can be repudiated by a minor or, after he reaches eighteen, repudiated within a reasonable time (on the problematic grant of a lease to a minor, see

other party, the Privy Council in *Hart v. O'Connor* (1985) held that a contract will arise, see 3.61;²⁴ as for 'legal persons', the company must be validly formed.

3. THE OBJECTIVE PRINCIPLE

- 1.10 This principle is a fundamental and pervasive aspect of contract law (for further detail, 3.57 ff). A person's words or conduct must be interpreted in the manner in which another might objectively and reasonably understand them.²⁵ As Lord Reid said in *McCutcheon v. David MacBrayne Ltd* (1964):²⁶ 'the judicial task is not to discover the actual intentions of each party; it is to decide what each was reasonably entitled to conclude from the attitude of the other.' Thus, the objective principle concerns the following matters: Is there a contract? If so, on what terms? Has the contract been varied or terminated by consensus? Has a party repudiated the agreement? Has the other party accepted that repudiation? Has a voidable contract been 'affirmed' by a party?

4. OVERVIEW OF CONTRACTUAL DOCTRINES

- 1.11 Contracts are legally enforceable agreements involving two or more parties. The agreement can involve one party assuming an obligation only if the other does something (or refrains from something): a so-called 'unilateral contract'. An example is an offer of reward payable only if the other party supplies desired information. But most contracts involve reciprocal obligations: a so-called 'bilateral contract'; for example, to sell and buy, to insure and pay the premium, to hire out and to pay the hire charge, to work and to pay a salary, etc.
- 1.12 Many contractual obligations are promises to do something, or to pay money, or to transfer property. Occasionally, a party might undertake to refrain from doing something, such as not to work for a rival employer for a specified period. In short, most promises are forward-looking commitments to do, pay, transfer or abstain. But there are two main variations. A contractual assurance need not involve a promise of *future* conduct (or abstention). Thus, a 'warranty' is an assurance that something is the case, or has been the case. Another variation is that a promise need not concern the promisor's own primary

Hammersmith and Fulham London Borough Council v. Alexander-David [2009] EWCA Civ 259; [2009] 3 All ER 1098; (4) all other types of contract (e.g. a contract of insurance or a trading contract, or a contract for a luxury item not within the scope of 'necessaries') are not binding on the minor unless he ratifies the transaction after reaching eighteen: *Chitty on Contracts* (30th edn, London, 2008), 8-042 ff; (5) section 3 of the Minors' Contracts Act 1987 permits the court to order restitution of 'any property acquired by the [minor] under the contract, or any property representing it', even if the minor had not lied about his age, and this provision applies to all contracts other than those at (1) and (2).

24 *Hart v. O'Connor* [1985] 2 All ER 880, PC; however, where the incapax's property is subject to the control of the court, under sections 15 ff of the Mental Capacity Act 2005, transactions which would be inconsistent with the court's control of those assets will be void as against that party; *Chitty on Contracts* (30th edn, London, 2008), 8-073, and *Treitel* (12th edn, London, 2007), 12-056, 12-057.

25 Lord Steyn, 'Contract Law: Fulfilling the Reasonable Expectations of Honest Men' (1997) 113 LQR 433.

26 [1964] 1 WLR 125, HL; see also *Shogun Finance Co. Ltd v. Hudson* [2003] UKHL 62; [2004] 1 AC 919, HL, at [183].

conduct. Thus, a guarantee (5.06, 5.18) is a surety's undertaking (normally) to indemnify a creditor if a debtor fails to satisfy a debt owed, or becoming due, to that creditor.

- 1.13 Some elements of basic contract law will now be explained. Formation of contract requires analysis in terms of offer and acceptance (chapter 3); certainty (chapter 4); intent to create legal relations (chapter 6); absence of a vitiating factor rendering the contract either void (common law mistake, chapter 10) or voidable (misrepresentation, duress, undue influence or unconscionability, chapter 11).
- 1.14 An agreement must either be supported by consideration (chapter 5) or contained in a 'deed': a deed is a formal written contract, which is normally gratuitous (see also 5.03 ff). The requirements for a valid deed are:²⁷ (1) the statement must be in writing; (2) this document must be declared to be a deed; (3) the document must be signed by the promisor (the 'covenantor'); (4) the document must be witnessed by another; and (5) the document must be 'delivered' (this word is misleading because the covenantor need not physically transfer the deed to the covenantee: it is enough that there is conduct indicating that the covenantor intends to be bound by it).²⁸
- 1.15 In general, contracts do not need to be in writing or comply with special formality (thus, an agreement for the purchase of a £10m ship or a £20m – inevitably over-priced – English footballer can be made without writing). The main exceptions, where a contract must be in writing or formalised, are agreements for the creation or transfer of interests in land (see also 5.07 ff) and guarantees (5.06, 5.18). Many contractual obligations are express, whether oral or written (for an overview, see 12.01 ff). But implied terms (chapter 13) are readily found as a result of statute or common law doctrine.
- 1.16 An agreement might be expressly 'subject to contract' (12.04; also 1.16, 2.07, 4.21, 6.06), so that it does not create any legally binding duties. Or an agreement might be subject to so-called 'conditions precedent' (12.02; see also 1.16, 10.07, 10.10, 14.29). For example, the contract might be contingent upon a third party, such as a government minister or planning authority, giving permission which is vital to the relevant transaction. Sometimes one party might agree to exercise best or reasonable endeavours to apply for such permission (2.10).
- 1.17 A contracting party's unexcused failure to perform, or his defective performance, constitutes a breach (chapter 17). The other party has a range of possible remedies in respect of breach (18.02 for an overview): orders to compel agreed performance (a claim in debt, 18.03; or, exceptionally, recourse to equitable and coercive relief by injunction, 18.20; or

²⁷ Section 1(2) and (3) of the Law of Property (Miscellaneous Provisions) Act 1989; as amended by Article 7(3) of the Regulatory Reform (Execution of Deeds and Documents) Order 2005 (SI 2005 No. 1906); *Treitel* (12th edn, London, 2007), 3-164 ff; *Bolton Metropolitan Borough Council v. Torkington* [2004] Ch 66, CA; *Chitty on Contracts* (30th edn, London, 2008), 1-087.

²⁸ *Treitel* (12th edn, London, 2007), 3-166.

specific performance, 18.13); claims for damages at common law (18.23); restitutionary claims in respect of the guilty party's unjust enrichment (18.51); declarations that the guilty party is in breach (18.62) (or the award of merely nominal damages, 18.23 at (2), that is, a token amount designed to register that there has been a breach of contract or commission of a tort); self-help measures (forfeiture of a deposit, 19.27); or a stipulated right to liquidated damages (19.02); or a possible right to repossess property (17.40) or to withhold reciprocal performance (17.51 ff).

- 1.18 A party's non-performance or defective performance might be excused by an exclusion clause (chapter 15) or under the common law doctrine of frustration (chapter 16). Frustration applies if the contractual situation has been drastically affected by a change of circumstances subsequent to the agreement's formation. It will not be enough that one party has experienced unforeseen price increases, even if they are very large. Nor is it enough that other changes have occurred which severely hamper his performance, or which render the transaction highly unattractive to him.
- 1.19 The agreement *at* common law does not confer rights of enforcement on a third party (for a summary, 7.01). Nor does it impose obligations on a third party (for a summary, 7.02). The main qualifications upon these fundamental propositions of 'privity of contract' are: a third party might acquire rights, including a right to require performance, by a trust of a promise (7.12); and the Contracts (Rights of Third Parties) Act 1999 (7.34) might enable the third party to take the benefit of the contract and sue the promisor for non-performance, or the third party might be permitted under the same Act to take the benefit of an exclusion clause. Alternatively, the benefit of the contract might be assigned. If so, the assignee acquires a direct right of action against the promisor (chapter 8).
- 1.20 An agreement can be reconstituted or varied in various ways:
- (1) by waiver or estoppel, at common law or in equity, suspending or modifying the agreement (5.33 ff);
 - (2) by a variation supported by consideration;
 - (3) by a variation formalised by deed;
 - (4) by the substitution of a new agreement between the same parties in one of two ways:
 - (a) either by 'transaction' novation, in which the first contract is replaced by a second contract between the same parties; or
 - (b) by 'new party' novation, in which one of the parties to the original contract is substituted by a new third party; thus a contract between A and B is replaced by a contract between A or B and C, a new party (8.12 at (1)).

On these two forms of novation, see the remarks in *Scarf v. Jardine* (1882) by Lord Selborne LC.²⁹

²⁹ (1882) LR 7 App Cas 345, 351, HL, *per* Lord Selborne LC.

- 1.21 An agreement can be discharged or terminated in various ways: first, by performance in full (unhappily for lawyers, the commonest situation); secondly, a contract might be terminated without a breach by either side, if a party exercises a right to cancel the contract explicitly or implicitly contained in the agreement (on termination clauses,³⁰ 16.30, 17.04); thirdly, by the occurrence of an event covered by an *express* 'condition subsequent' clause contained in the contract ('conditions subsequent', 10.11); fourthly, by reason of supervening illegality or frustration which brings the contract to an end by operation of law (chapter 16); fifthly, by consensual termination of the agreement; sixthly, by merger of outstanding obligations in a judgment.³¹ The seventh way in which a contract might be terminated involves an innocent party choosing to end the contract because of the other's serious breach. This topic is complex (17.18 ff). The innocent party has the choice of ending the contract if: (1) the other party has repudiated the agreement, by unequivocally declaring or indicating that he does not intend to perform his obligations; or (2) the other party has committed a breach of a condition (a promissory term which is so labelled by the parties, or so classified by statute or judicial decision, or which must be construed as such, having regard to its importance); or (3) a clause which, when breached, is expressly classified by the agreement as equivalent to a condition; or (4) there is a really serious breach of an innominate term so as to deprive the innocent party of substantially the entire expected performance.

5. CONTRACT AND TORT LAW³²

- 1.22 Many contractual obligations are strict in the sense that a party can be in breach of agreement even though he has exercised all reasonable care to try to satisfy his obligation. However, some contractual obligations are less demanding and merely require the exercise of reasonable care, or a similar standard (see 17.06 and 18.42). Normally in a contract for the performance of professional services, the performing party will owe merely an obligation to exercise due care, rather than to guarantee the success of the task: 17.06.

The distinction between 'a duty to achieve a specific result' and 'a duty of best efforts' is drawn within the (non-binding) UNIDROIT's *Principles of International Commercial Contracts* (2004), Article 5.1.4 and 5.1.5.³³

- 1.23 In some situations, the relationship underlying the agreement simultaneously involves a common law or extra-contractual duty to exercise reasonable care (generally on the imposition of duties of care in tort in respect of economic loss, 5.17). There might then be overlapping rights and duties in contract and in tort. This is true of many professional

30 S. Whittaker, 'Termination Clauses', in A. Burrows and E. Peel (eds.), *Contract Terms* (Oxford, 2007), chapter 13.

31 *Director General of Fair Trading v. First National Bank plc* [2002] 1 AC 481, HL.

32 A. S. Burrows, *Understanding the Law of Obligations* (Oxford, 1998), chapters 1, 2 and 8.

33 2nd edn, Rome, 2004; see M. J. Bonell (ed.), *The UNIDROIT Principles in Practice: Case Law and Bibliography on the UNIDROIT Principles of International Commercial Contracts* (2nd edn, Ardsley, NY, 2006), 255–60; S. Vogenauer and J. Kleinheisterkamp (eds.), *Commentary on the UNIDROIT Principles of International Commercial Contracts* (Oxford, 2009), 548–54.

relationships. The House of Lords affirmed in *Henderson v. Merrett Syndicates Ltd* (1995)³⁴ that, when a contractual duty of care overlaps with an essentially similar duty of care imposed by the tort of negligence, a claimant can select whichever cause of action he prefers, or indeed plead both (so-called ‘concurrence’ of claims, 17.06; on remoteness of damage, 18.42;³⁵ on contributory negligence, 18.50). The main difference between these ‘concurrent’ sources of claim (‘causes of action’) is the commencement of the limitation period: ‘in cases of breach of contract the cause of action arises at the date of the breach of contract’; but ‘in tort the cause of action arises, not when the culpable conduct occurs, but when the plaintiff first sustains damage’.³⁶ The limitation periods for breach of contract are six years for ordinary (‘simple’)³⁷ contracts (oral, written, and partly written contracts, other than deeds or covenants) and twelve years for deeds (for the latter, 5.03).³⁸ Tort also interrelates with the law of contract in the field of pre-contractual misrepresentations,³⁹ where the torts of negligent misstatement and deceit provide sources of damages for inaccurate statements (9.12, 9.15). (There has been discussion of the ‘contract/tort interface’ in recent US literature.)⁴⁰

6. CONTRACT AND RESTITUTION OR UNJUST ENRICHMENT⁴¹

- 1.24 Contract law often interacts with the law of restitution or unjust enrichment, a category of obligations now recognised to subsist separately from contract and tort.⁴² Overlap between restitution and contract will be noted not just in the chapter on remedies (18.52 ff), but also in respect of contracts which ‘fail to materialise’ (2.04) and rescission following misrepresentation (9.18 ff). Restitutionary claims are based on the defendant’s unjust enrichment. Most restitutionary remedies become available without the need to show a contractual breach. However, breach of contract is an essential element in one restitutionary remedy: the remedy of ‘equitable account’ (see the *Attorney-General v. Blake*⁴³ line of cases, 18.56). A restitutionary claim is not made to remedy a claimant’s loss. Instead, it is a claim in respect of the defendant’s enrichment at the

34 [1995] 2 AC 145, HL.

35 On aspects of the remoteness tests in contract and tort, see A. Kramer, in D. Saidov and R. Cunnington (eds.), *Contract Damages: Domestic and International Perspectives* (Oxford, 2008), chapter 12.

36 *Nykredit Mortgage Bank plc v. Edward Erdman Group (No. 2)* [1997] 1 WLR 1627, 1630, HL.

37 Section 5 of the Limitation Act 1980.

38 Section 8 of the Limitation Act 1980 refers to actions on ‘specialties’, for example, a deed.

39 J. Cartwright, ‘Liability in Tort for Pre-Contractual Non-Disclosure’, in A. Burrows and E. Peel (eds.), *Contract Formation and Parties* (Oxford, 2010).

40 R. Kreitner, ‘Fault at the Contract/Tort Interface’ (2009) 107 *Michigan Law Review* 1533.

41 Leading works include: T. Baloch, *Unjust Enrichment and Contract* (Oxford, 2009); A. Burrows, *The Law of Restitution* (2nd edn, London, 2002); R. Goff and G. H. Jones, *The Law of Restitution* (7th edn, London, 2007); G. Virgo, *The Principles of the Law of Restitution* (2nd edn, Oxford, 2006); and A. Burrows, E. McKendrick and J. Edelman, *Cases and Materials on the Law of Restitution* (2nd edn, Oxford, 2007).

42 A. S. Burrows, *Understanding the Law of Obligations* (Oxford, 1998), chapters 1 and 3.

43 [2001] 1 AC 268, HL; J. Edelman, *Gain-Based Damages* (Oxford, 2002), chapter 5; E. McKendrick, in A. Burrows and E. Peel (eds.), *Commercial Remedies: Current Issues and Problems* (Oxford, 2003), 93–119; A. S. Burrows, *Remedies for Torts and Breach of Contract* (3rd edn, Oxford, 2004), 395–407; R. Goff and G. H. Jones, *The Law of Restitution* (7th edn, London, 2007), 20–024 ff; D. Howarth, in S. Hedley and M. Halliwell (eds.), *The Law of Restitution* (London, 2002), 11.7 to 11.31.

claimant's expense (for example, if the claimant has transferred money to, or conferred the benefit of services upon, the defendant), or at any rate enrichment arising as a result of breach of duty or violation of the claimant's rights. Thus, the enrichment can constitute money or services or goods. The cause of action based on restitution or unjust enrichment can take various forms: it might be that the benefit was conferred as a result of the claimant's mistake of fact or law; or that there was a (total) failure of consideration, or duress, or undue influence, or abuse of fiduciary relationship,⁴⁴ or an unjustified tax demand. There are three main forms of restitutionary relief relevant to contract law (18.51 ff): (1) money recovered for a total failure of consideration; (2) recovery in respect of goods or services; and (3) disgorgement of gains made in breach of contract.

7. COMMON LAW AND EQUITY

- 1.25 The Supreme Court of Judicature Acts 1873 and 1875 enabled the High Court and county courts to administer both common law and equity in the same case (see also 18.31). Even so, the distinction between common law and equity remains important for the exposition of contract law. Thus, in the modern law, there is still a fundamental distinction between common law and equitable doctrines⁴⁵ and remedies. Examples of this classification are: the equitable doctrines of rectification (9.16), undue influence, unconscionability (on these see chapter 7), and equitable bars upon rescission (6.22); and the common law doctrines of 'mistake' or duress (on these see chapters 6 and 7). As for remedies for breach of contract (18.02 for an overview), the money claims for debt and damages are both common law remedies (for a claim in debt, see 18.03; for damages at common law, see 18.23), but injunctions (18.20), specific performance (18.13) and an account of profits (18.56) are 'equitable'. Some recent decisions have tended to diminish the common law / equitable distinction.⁴⁶ The distinction between common law and equity remains the 'bed-rock' within English private law,⁴⁷ and in other common law jurisdictions. It will prove hard to eradicate. However, a debate has emerged on whether English law should 'move on' and jettison this historical baggage. Andrew Burrows has strongly advocated abandonment of this distinction.⁴⁸ But it is likely that this distinction will endure for many

44 *Calvert v. William Hill Credit Ltd* [2008] EWCA Civ 1427; [2009] Ch 330, at [53]; *Parker and Mellows: The Modern Law of Trusts* (9th edn, London, 2008), 10-048 ff; J. Edelman, 'When Do Fiduciary Duties Arise?' (2010) 126 LQR 302.

45 In the USA, the fact that the remedy of injunction is 'equitable' places a claim for such relief outside the constitutional guarantee of jury trial: see G. Hazard and M. Taruffo, *American Civil Procedure* (New Haven, CT, 1993), 130.

46 E.g. no separate doctrine of shared 'equitable' mistake, *The Great Peace* [2003] QB 679, CA; and no separate equitable principles of construction of contracts, *BCCI v. Ali* [2001] UKHL 8; [2002] 1 AC 251, at [17].

47 E.g. on the question whether a beneficial (as distinct from legal) owner has title to sue in the tort of negligence, see *Shell UK Ltd v. Total UK Ltd* [2010] EWCA Civ 180; [2010] 3 All ER 1192 (beneficial owner competent to sue if joins legal owner as co-claimant).

48 Inaugural Oxford lecture, A. S. Burrows, 'We Do This at Common Law But That in Equity' (2002) 22 OJLS 1.

years, and that even a codification of contract law would merely echo the fundamental conceptual distinctions between common law and equity.

- 1.26 There is scope for confusion because the expression ‘common law rule’ is sometimes used to denote the distinction between judge-made law (both common law and equitable doctrine) and legislation. An example of a judge-made rule observed at ‘common law’ and in ‘equity’ is the doctrine of consideration. This rule prevents a person from suing a defendant for breach of contract (in the absence of a formal contract known as a ‘deed’) unless the claimant has provided some element of bargain at the defendant’s request (on deeds, see 5.03; generally on the consideration doctrine, see chapter 5). The consideration rule was observed both by the pre-Judicature Act (see 1.25 above) common law courts (Queen’s Bench, Court of Common Pleas, Exchequer Court) and the Court of Chancery (‘Court of Equity’). The modern courts continue to adhere to it. In short, ‘common law’ is sometimes the antithesis to ‘equity’. However, ‘common law’ doctrine is sometimes the antithesis to ‘statutory’ or ‘legislative’, and in this sense the expression ‘common law’ embraces common law and equitable doctrine, because both are the product of judicial law-making.

8. GOOD FAITH

- 1.27 This topic has produced a vast literature,⁴⁹ and it is further examined at 21.03 to 21.18. This concept applies potentially both to performance of contracts and to the pre-contractual phase. ‘Good faith’ in the performance of contracts is a prominent feature of civil law systems of contract law (for example, section 242 of the German Civil Code; Article 1134 of the French Civil Code; and Articles 1337, 1366 and 1375 of the Italian Civil Code); and the same concept has been adopted in the USA, both in the *Restatement of the Law Second, Contracts* (1981), section 205, and in the Uniform Commercial Code, section 1-203. Furthermore, UNIDROIT, Article 1.7,⁵⁰ PECL,

49 J. Beatson and D. Friedmann (eds.), *Good Faith and Fault in Contract Law* (Oxford, 1995), chapter 2 (N. Cohen, Israel), chapter 6 (E. A. Farnsworth, USA) and chapter 7 (W. Ebke and B. M. Steinhauer, Germany); A. Berg, ‘Promises to Negotiate in Good Faith’ (2003) 119 LQR 357; R. Brownsword, *Contract Law: Themes for the Twenty-First Century* (2nd edn, Oxford, 2006), chapter 5 (also as R. Brownsword, in M. Furmston (ed.), *The Law of Contract* (3rd edn, London, 2007), chapter 1); S. J. Burton and E. G. Andersen, *Contractual Good Faith* (Boston, 1995); M. Clarke, ‘The Common Law of Contract in 1993: Is There a General Doctrine of Good Faith?’ (1993) 23 *Hong Kong Law Journal* 318; H. G. Collins, ‘Good Faith in European Contract Law’ (1994) 14 OJLS 229; H. G. Collins, *The Law of Contract* (4th edn, 2003), chapters 10 and 15; A. Forte (ed.), *Good Faith in Contract and Property Law* (Oxford, 1999); E. McKendrick, *Contract Law: Text, Cases and Materials* (4th edn, Oxford, 2010), chapter 15; J. O’Connor, *Good Faith in English Law* (Aldershot, 1990), chapter 3; Lord Steyn, ‘Contract Law: Fulfilling the Reasonable Expectations of Honest Men’ (1997) 113 LQR 433; G. Teubner, ‘Legal Irritants: Good Faith in British Law or How Unifying Law Ends Up in New Divergences’ (1998) 61 MLR 11; R. Zimmermann and S. Whittaker (eds.), *Good Faith in European Contract Law* (Cambridge, 2000); and H. MacQueen and R. Zimmermann (eds.), *European Contract Law: Scots and South African Perspectives* (Edinburgh, 2006), 17–18 (Zimmermann) and chapter 2 (MacQueen).

50 M. J. Bonell (ed.), *The UNIDROIT Principles in Practice: Case Law and Bibliography on the UNIDROIT Principles of International Commercial Contracts* (2nd edn, Ardsley, NY, 2006), 83 ff; S. Vogenauer and J. Kleinheisterkamp (eds.), *Commentary on the UNIDROIT Principles of International Commercial Contracts* (Oxford, 2009), 165 ff.

Article 2:201, and the *Common Frame of Reference*, Article III-1:103,⁵¹ all adopt this principle. But ‘good faith’ is not an explicitly recognised general doctrine in English contract law.⁵² As Bingham LJ said in *Interfoto Picture Library Ltd v. Stiletto Visual Programmes Ltd* (1989):⁵³ ‘English law has, characteristically, committed itself to no such overriding principle but has developed piecemeal solutions in response to demonstrated problems of unfairness.’ The author’s contentions at 21.03 ff will be: (1) in England, the principle of good faith is not required in the context of pre-contractual negotiations (for current law, chapter 2) because of the highly developed and fertile array of existing doctrines; but (2) as for ‘good faith’ as a general principle governing performance of contracts, the case is more evenly balanced. In the case of (2), there would be only a slight benefit in making such a change. The courts would be unlikely to use the concept dynamically. The inevitable anxiety and uncertainty experienced within the legal profession, when advising their clients, might outweigh the possible and marginal benefits of such a change.

9. EUROPEAN UNION LAW

- 1.28 English law is subject to various EU Directives and Regulations.⁵⁴ The most important example of these is the Unfair Terms in Consumer Contracts Regulations 1999 (15.33). These implement the European Council Directive aimed at achieving harmony in the legal treatment of consumer contracts.⁵⁵ Hugh Collins⁵⁶ has also noted the wide impact of the EU Directive on Unfair Commercial Practices (2005),⁵⁷ implemented by the Consumer Protection from Unfair Trading Regulations 2008.⁵⁸

10. TRANSNATIONAL CONTRACT LAW⁵⁹

- 1.29 This topic is considered in detail in chapter 21.

51 *Principles, Definitions and Model Rules of European Private Law Draft Common Frame of Reference*, ed. Christian von Bar and Eric Clive (6 vols., Oxford University Press/Sellier, 2010).

52 E. McKendrick, *Contract Law: Text, Cases and Materials* (4th edn, Oxford, 2010), chapter 15 (examining R. Brownsword’s sophisticated discussion in M. Furmston (ed.), *The Law of Contract* (3rd edn, London, 2007), 1.79 ff).

53 [1989] QB 433, 439, CA.

54 E.g. Consumer Protection (Distance Selling) Regulations 2000 (SI 2000 No. 2334); and the EU Directive on Electronic Commerce (Directive 2000/31/EC); S. Whittaker, ‘A Framework of Principle for European Contract Law’ (2009) 125 LQR 617; S. Weatherill, ‘An Ever Tighter Grip: The European Court’s Pro-Consumer Interpretation of the EC’s Directives Affecting Consumer Law’, in *Liber Amicorum Guido Alpa: National Private Law Systems* (London, 2007), 1037.

55 Giving effect to Directive 93/13/EEC.

56 H. G. Collins, ‘Harmonisation by Example: European Laws against Unfair Commercial Practices’ (2010) 73 MLR 89–118.

57 Directive 2005/29/EC.

58 Consumer Protection from Unfair Trading Regulations 2008 (SI 2008 No. 1277).

59 See especially H. MacQueen and R. Zimmermann (eds.), *European Contract Law: Scots and South African Perspectives* (Edinburgh, 2006), chapter 1; R. Goode, *Commercial Law in the Next Millennium* (London, 1998) (Hamlyn Lecture Series, 1997), 88–105.

11. BIBLIOGRAPHY

- 1.30 A bibliography is set out at the end of this book. Most of the chapters also include (after the introductory paragraph) a list of selected further reading on the topics covered in those chapters.

12. A WHO'S WHO OF CONTRACT LAW

- 1.31 A who's who of contract law is set out in the appendix to this book. This gives short biographies of fifty of the leading figures in the history and development of English contract law.

II

Formation

Chapter contents

1. Introduction *para. 2.01*
2. Abortive pre-contractual negotiations *para. 2.03*
3. Negotiation agreements prior to formation of the
main contract *para. 2.06*
4. Agreements ancillary to a settled agreement *para. 2.10*
5. Mediation agreements *para. 2.13*

2

The pre-contractual phase

1. INTRODUCTION¹

2.01 Summary of main points

- (1) The principle of freedom of contract (1.08) permits negotiating parties to 'walk away' from a proposed deal, provided they have not already committed themselves in law to a binding agreement.
- (2) In the absence of a binding contract, a person's requested performance, whether delivery of goods or performance of services, can give rise to a restitutionary obligation to pay the reasonable market value of the relevant performance (generally on this type of restitutionary claim: 2.04, 18.55).
- (3) In the situation just mentioned, the law is presently defective in not allowing the recipient of the relevant performance to require a reduction in the financial award to reflect slow performance (2.04).
- (4) Further points are summarised at 2.06.

A. Berg, 'Promises to Negotiate in Good Faith' (2003) 110 LQR 357–63

¹ Cheshire, *Fifoot and Furmston's Law of Contract* (15th edn, Oxford, 2007), 85–91; E. McKendrick, 'Work Done in Anticipation of a Contract Which Does Not Materialise', in W. Cornish, R. Nolan, J. O'Sullivan and G. Virgo (eds.), *Restitution: Past, Present and Future* (Oxford, 1998), chapter 11; M. Spence, *Protecting Reliance: The Emergent Doctrine of Equitable Estoppel* (Oxford, 1999), 87–106; D. K. Allen, 'Pre-Contractual Liability', in J. Gardner (ed.), *UK Law in the 1990s* (London, 1990), 90 ff; J. Dietrich, 'Classifying Pre-Contractual Liability: A Comparative Analysis' (2001) LS 153; R. Zimmermann and S. Whittaker (eds.), *Good Faith in European Contract Law* (Cambridge, 2000), 236–57; P. Giliker, *Pre-Contractual Liability in English and French Law* (Nijmegen, 2002); P. Giliker, 'A Role for Tort in Pre-Contractual Negotiations? An Examination of English, French, and Canadian Law' (2003) 52 ICLQ 968.

S. Ball, 'Work Carried Out in Pursuance of Letters of Intent – Contract or Restitution?' (1983) 99 LQR 572, especially 576–9, 581–2

P. Giliker, 'A Role for Tort in Pre-Contractual Negotiations? An Examination of English, French and Canadian Law' (2003) 52 ICLQ 969, especially 989 to end

2.02 English law has fashioned an intricate set of rules governing the pre-contractual context. Readers hoping to find a single formula, such as a pre-contractual duty to negotiate in good faith, will find English law lacking in such simplicity. Our courts have used a 'Swiss army knife' for this purpose, rather than a single blade. But it will be apparent to those who are willing to read between the lines of the judgments explained in this chapter that English law is not allergic to notions of pre-contractual fair dealing or responsibility for culpable or bad faith rupture of negotiations. On the contrary, English law energetically intervenes to correct an injustice in this context. It will also be convenient here to examine the related topic of mediation clauses (2.13), even though such clauses normally arise from within an existing contract.

2. ABORTIVE PRE-CONTRACTUAL NEGOTIATIONS

2.03 Freedom of contract involves freedom not to contract (generally on the principle of freedom of contract, see 1.08). As Lord Ackner said in *Walford v. Miles* (1992):² 'Each party to [pre-contractual] negotiations is entitled to pursue his (or her) own interest, so long as he avoids making misrepresentations. To advance that interest he must be entitled, if he thinks it appropriate, to ... withdraw [with impunity].'³ However, the pre-contractual zone is not a lawless jungle. Some civil law jurisdictions police the pre-contractual zone on the basis of general principles of good faith or fair dealing, or a wide notion of *culpa in contrahendo* (fault during the process of bargaining). For example, Israeli law uses the principle of good faith, drawing upon German law.⁴ But English courts do not recognise a general doctrine of fault in bargaining,⁵ nor a general doctrine of good faith negotiation. Traditionally, English lawyers regard 'good faith' as an unattractively vague concept (for 'soft law' codes on this, such as UNIDROIT's *Principles of International Commercial Contracts* (2004)⁶ and the *Principles of European Contract Law*, see 21.02;⁷ generally on English antipathy to 'good faith' as an

2 [1992] 2 AC 128, HL.

3 See also Article 28 of the Contract Law of the Dubai International Financial Centre: www.difc.ae/laws-regulations/.

4 N. Cohen, in J. Beatson and D. Friedmann (eds.), *Good Faith and Fault in Contract Law* (Oxford, 1995), 32.

5 P. Giliker, 'A Role for Tort in Pre-Contractual Negotiations? An Examination of English, French, and Canadian Law' (2003) 52 ICLQ 968; J. Cartwright and M. Hesselink (eds.), *Precontractual Liability in European Private Law* (Cambridge, 2008); J. Cartwright, 'The English Law of Contract: Time for Review?' (2009) 17 *European Review of Private Law* 155, 156; as for French law, see J. Ghestin, 'La Responsabilité Délictuelle pour Rupture des Pourparlers ...', in *Liber Amicorum Guido Alpa: National Private Law Systems* (London, 2007), 436.

6 2nd edn, Rome, 2004; see M. J. Bonell (ed.), *The UNIDROIT Principles in Practice: Case Law and Bibliography on the UNIDROIT Principles of International Commercial Contracts* (2nd edn, Ardsley, NY, 2006), 83 ff; S. Vogenauer and J. Kleinheisterkamp (eds.), *Commentary on the UNIDROIT Principles of International Commercial Contracts* (Oxford, 2009), 165 ff.

7 O. Lando and H. Beale (eds.), *Principles of European Contract Law* (The Hague, 2000).

implicit contractual norm, see 21.03 ff). Instead, English law uses a mix of common law and equitable doctrines to protect a party to negotiations. As we shall see, English law can intervene to prevent unjust enrichment, or to remedy deceit or other unfair dealing.

- 2.04 *Unjust enrichment or restitutionary relief.* On the facts of the *British Steel* case (1984; for further comment on the case, see 18.55), Robert Goff J held that there was no contract because there had been a failure of offer and acceptance⁸ (this case was approved, and examined in detail, by the Supreme Court in the *RTS* case, 2010, see 4.21). In the *British Steel* case, the claimant had delivered a large number of special ‘steel nodes’ for use by the defendant construction company in erecting a building. Eventually all the nodes had been supplied. But the defendant alleged that the claimant had delivered them too slowly and in the wrong sequence and that, as a result, the defendant had suffered delay in completing its project. The dispute concerned both the main claim for payment (the market value of the goods was £229,832), and a counter-claim against the claimant for compensation in respect of the defendant’s commercial loss caused by the alleged slow and haphazard delivery of these materials (£867,735). But Goff J gave two reasons for finding that no contract had arisen. Two matters had been unresolved during the parties’ negotiations: first, the supplier’s possible liability for consequential loss (for example, because of slow delivery); and, secondly, the price to be paid.⁹ For either reason, the requirements of offer and acceptance had not been satisfied. Goff J also held that it made no difference that a letter of intent had been issued (relatedly, see *Kleinwort Benson v. Malaysian Mining* (1989) at 6.13).

Goff J’s finding on this point is summarised as follows:¹⁰

[The proposed contract] was plainly in a state of negotiation, not least on the issues of price, delivery dates, and the applicable terms and conditions. In these circumstances, it is very difficult to see how BSC, by starting work, bound themselves to any contractual performance. No doubt it was envisaged by CBE at the time they sent the letter that negotiations had reached an advanced stage, and that a formal contract would soon be signed; but, since the parties were still in a state of negotiation, it is impossible to say with any degree of certainty what the material terms of that contract would be.

Despite finding that no contract had arisen in this case, Goff J awarded the claimant the market value of the goods (£229,832), on the basis of restitution, an extra-contractual cause of action (18.51). Goff J said:¹¹

8 *British Steel Corporation v. Cleveland Bridge and Engineering Company* [1984] 1 All ER 504; S. Ball, ‘Work Carried Out in Pursuance of Letters of Intent – Contract or Restitution?’ (1983) 99 LQR 572; E. McKendrick, ‘The Battle of the Forms and the Law of Restitution’ (1988) 8 OJLS 197, at 212, 215 and 217; A. Burrows, *The Law of Restitution* (3rd edn, London, 2004), 372–81; J. Edelman, ‘Liability in Unjust Enrichment Where a Contract Fails to Materialise’, in A. Burrows and E. Peel (eds.), *Contract Formation and Parties* (Oxford, 2010).

9 [1984] 1 All ER 504, 509–11, *per* Goff J.

10 *Ibid.*, at 510.

11 *Ibid.*, at 511; generally on restitutionary relief in this context, see *MSM Consulting Ltd v. United Republic of Tanzania* [2009] EWHC 121 (QB), at [171], *per* Clarke J (distilling principles, with the assistance of

Both parties confidently expected a formal contract to eventuate. In these circumstances, to expedite performance under that anticipated contract, one requested the other to commence the contract work, and the other complied with that request. If thereafter, as anticipated, a contract was entered into, the work done as requested will be treated as having been performed under that contract; if, contrary to their expectation, no contract was entered into, then the performance of the work is not referable to any contract the terms of which can be ascertained, and the law simply imposes an obligation on the party who made the request to pay a reasonable sum for such work as has been done pursuant to that request, such an obligation sounding in quasi contract or, as we now say, in restitution.

But Goff J could not make any allowance in respect of the counter-claim (the defendant's alleged commercial loss in receiving the nodes slowly and in the wrong order), because that counter-claim presupposed a breach of duty and hence a valid contract. In any event, Goff J said¹² that, even if there had been a contract on these facts, the supplier had delivered within a reasonable time. As for the allegation that there had been delivery out of sequence, he said that this claim would require an express term,¹³ and he chose not to comment further on this allegation.

And so the *British Steel* case vividly illustrates that restitution can be a second-best solution for the recipient of materials or work, where both parties have a grievance: restitution might confer victory on the supplier, who gains the full market value of the goods supplied; but there can be no correlative victory for the defendant in respect of the alleged slow performance. The restitutionary award made in this case is asymmetrical, operating solely in favour of the performer. In response to the *British Steel* case, Ball (1993) contended that the courts should adopt a more flexible approach to finding a contract, and he further suggested that businessmen would welcome such an approach as pragmatic and reasonable.¹⁴ However, the objection to this is that imposing a contract in the teeth of the parties' failure to agree would offend the principle of freedom of contract (1.08): parties to negotiations should not be treated as having reached final agreement if it is clear that they have yet to finalise the agreement and have instead reserved to themselves the task of establishing final consensus. Consistent with this, Goff J decided (see the first passage quoted above) that the parties in the *British Steel* case had clearly not settled major difficulties in their negotiations. They had decided to proceed with performance but only in the hope that a final contract would take shape later.

However, it might be possible in some situations to impose a contractual solution on the basis that the parties' dealings *have implicitly overridden the negotiation snag or implicitly waived a 'subject to contract' bar*. It was on this basis that the *British Steel*

Nicholas Strauss QC's decision in *Countrywide Communications Ltd v. ICL Pathway Ltd* [2000] CLC 324, 349, noted by P. Jaffey, [2000] *Restitution Law Review* 270–5).

12 [1984] 1 All ER 504, 512.

13 *Ibid.*

14 S. Ball, 'Work Carried Out in Pursuance of Letters of Intent – Contract or Restitution?' (1983) 99 LQR 572; similarly, J. O'Sullivan and J. Hilliard, *The Law of Contract* (4th edn, Oxford, 2010), 5.13 ff.

case was distinguished in *RTS Flexible Systems Ltd v. Molkerei Alois Müller GmbH* (2010).¹⁵ In the latter case, the Supreme Court rationalised the *British Steel* case as an example of unresolved points of difference which precluded a finding of a contract, and where non-contractual performance was understood to have proceeded pending a final and completely agreed set of terms. By contrast, in the *RTS* case, the parties had agreed on all the essential terms and had simply failed to sign the formal contract, as they had contemplated that they would. The Supreme Court held that the parties' decision to carry out nearly three-quarters of the contemplated transaction could be objectively construed as a tacit joint waiver of the 'subject to contract' bar which the parties had earlier expressly imposed, but which they had now implicitly lifted (the *RTS* case is examined in detail at 4.21).

Another possible approach (although not as attractive as the contractual route, just explained) would be to reduce the amount of the claimant's restitutionary claim to reflect the fact that performance was slow. But, perhaps regrettably, restitution law has yet to develop a method of making such a reduction for defective performance, including the present situation where goods have been delivered 'late' or 'out of sequence' (although Burrows, a leading commentator on the law of restitution, has attractively approved this possibility).¹⁶ A more flexible restitutionary approach is needed. After all, the defence of contributory negligence (18.50) requires the courts to work out on a rough-and-ready basis the claimant's damages, allowing a discount for his own culpable conduct. And, in the context of frustrated contracts, the Law Reform (Frustrated Contracts) Act 1943 (16.21) creates a flexible scheme for awarding a 'just sum', taking into account factors on both the claimant's side and his opponent's. However, it must be admitted that, even if this flexibility could be shown in the restitution context, the technique has its limits. On the facts of the *British Steel* case, this 'discount for defective performance' approach would have achieved an imperfect result: for the value of the counter-claim (approximately £868,000) greatly exceeded the reasonable value of the goods supplied (approximately £230,000).

- 2.05 *Proprietary estoppel*. This doctrine can be used to achieve justice in the pre- or extra-contractual zone. To avoid repetition, the reader is referred to the discussion at 5.64.

3. NEGOTIATION AGREEMENTS PRIOR TO FORMATION OF THE MAIN CONTRACT¹⁷

- 2.06 *Summary*. The following propositions will emerge from this section:

- (1) English law does not recognise as valid an agreement to negotiate in good faith or reasonably the terms of the main contract: in *Walford v. Miles* (1992), the House

¹⁵ [2010] UKSC 14; [2010] 1 WLR 753, at [55].

¹⁶ A. Burrows, *A Casebook on Contract* (2nd edn, Oxford, 2009), 77.

¹⁷ M. Furmston and G. J. Tolhurst, *Contract Formation: Law and Practice* (Oxford, 2010), 11.33 ff; E. Peel, 'The Status of Agreements to Negotiate in Good Faith', in A. Burrows and E. Peel (eds.), *Contract Formation and Parties* (Oxford, 2010).

- of Lords held that such an agreement is uncertain and void;¹⁸ one reason is that an obligation to bargain in good faith or reasonably is too vague; furthermore, courts would otherwise become embroiled in complicated inquiries into the reasons why negotiations broke down. It is submitted that *Walford v. Miles* was correctly decided, subject only to the unsettled suggestion, concerning negotiation agreements ancillary to valid contracts, summarised at (5) below.
- (2) Nor does English law uphold an obligation to use best reasonable endeavours to reach agreement on the main part of the proposed deal, for example, the nature of the subject matter or the price. As Millett LJ said in *Little v. Courage* (1995): ‘an undertaking to use one’s best endeavours to agree ... is no different from an undertaking to agree, to try to agree, or to negotiate with a view to reaching an agreement; all are equally uncertain and incapable of giving rise to an enforceable obligation.’¹⁹
 - (3) However, a so-called ‘lock out’ agreement for a fixed²⁰ period is valid (known also in practice as an ‘exclusivity agreement’).²¹ Thus, A and B can validly agree for consideration (in other words, for a price or something in return) that A or B, or both, will not negotiate with third parties (nor solicit offers, etc.); but the period of exclusivity must be fixed and not, for example, ‘a reasonable period’ or ‘for as long as necessary or reasonable’, otherwise the question of the reasonableness of one party’s withdrawal from negotiations would arise in a different guise.
 - (4) An agreement to use best endeavours to obtain planning permission, or an export licence, is also valid. Such ancillary obligations are designed to procure a specific external consent necessary for the achievement of the main transaction.²² It is not the same as an agreement to behave reasonably *vis-à-vis* the other main negotiating party.
 - (5) As discussed at 2.11, Longmore LJ’s *dicta* in *Petromec Inc. etc. v. Petroleo Brasileiro SA* (CA, 2005)²³ suggest that, *provided the main contract is valid, the courts might uphold an ancillary negotiation clause* requiring the parties in *good faith or reasonably* to negotiate aspects of the transaction; but this would be possible only if the court can discern a sufficiently objective criterion to regulate those further dealings; this *obiter* statement has yet to be confirmed to be the law.
 - (6) Furthermore, *when the main contract is valid*, the law will uphold an express ancillary clause imposing a duty of *performance in ‘utmost good faith’* by the parties; the effect of such a clause is to require the parties, *during performance*, to take action consistent with the achievement of the contract’s main purpose, or to desist from action which will stultify that purpose.²⁴

18 [1992] 2 AC 128, HL.

19 *Little v. Courage Ltd* (1995) 70 P & CR 469, 476, CA; affirmed, *London & Regional Investments Ltd v. TBI plc* [2002] EWCA Civ 355, at [39] and [40].

20 Applied in *Pitt v. PHH Asset Management Ltd* [1994] 1 WLR 327, CA.

21 *Walford v. Miles* [1992] 2 AC 128, 140D, HL.

22 *Little v. Courage Ltd* (1995) 70 P & CR 469, 476, CA; *Rae Lambert v. HTV Cymru (Wales) Ltd* [1998] FSR 874, CA.

23 [2005] EWCA Civ 891; [2006] 1 Lloyd’s Rep 121, at [115] to [121].

24 *Berkeley Community Villages Ltd v. Pullen* [2007] EWHC 1330, *per* Morgan J (and the *dictum* at [141] that an implied term to this effect might also arise).

- (7) The Privy Council in *Pratt Contractors Ltd v. Transit New Zealand* (2003) acknowledged as established law (including it seems in English law) that there is *an implied duty on the part of the invitor to conduct the tender process in good faith*²⁵ (3.51).
- (8) Finally, the law also upholds agreements to mediate disputes (2.13).²⁶

2.07 Agreement to negotiate main contract in good faith or reasonably. The House of Lords in *Walford v. Miles* (1992) decided that an agreement to negotiate in good faith or reasonably is uncertain and void.²⁷ The two main reasons given for this are, first, that bargaining in good faith (or reasonably) is too vague a concept for English use; secondly, it is suggested that the courts would otherwise become embroiled in complicated inquiries into the reasons why negotiations had broken down. The decision in the *Walford* case has been criticised,²⁸ and these views are considered at 2.09.

In *Walford v. Miles* (1992),²⁹ the parties had entered into a preliminary agreement to regulate the conduct of their negotiations for the sale of a photographic business. The defendant vendor promised, for consideration, to negotiate only with the claimant and not to negotiate with any third party. The main agreement for sale was expressly made 'subject to contract' and so had no legal effect. The proposed contract price for this sale was £2m. Because the vendor was ill, he did not want to have to assist in the business after it had been sold. For that reason, he sold the business to a third party for £2m, who would be able to take immediate control of the business (the vendor sensing that, if he sold it instead to the claimant, the vendor would remain involved during a substantial period of transition). In fact, this was a sale at an undervalue: the property was worth £3m. The claimant knew this, but had not told the defendant (nor was the claimant obliged to do so, according to established English doctrine, 3.66 ff).

At first instance, the judge awarded the claimant damages under two heads: (1) on the basis of misrepresentations made by the defendant, £700 for wasted expenditure; and (2) loss of bargain, £1m, being the difference between the property's real value and the contemplated contractual price. Both the Court of Appeal and the House of Lords upheld the award at (1) (although Bingham LJ in the Court of Appeal had doubted that the facts supported this finding of misrepresentation). However, point (2) was overturned both by a majority of the Court of Appeal (Bingham LJ dissenting) and by all five Law Lords.

25 [2003] UKPC 83; [2004] BLR 143; 100 Con LR 29.

26 *Cable & Wireless plc v. IBM United Kingdom Ltd* [2002] 2 All ER (Comm) 1041, *per* Colman J.

27 [1992] 2 AC 128, HL; see next note for literature on this case.

28 Lord Steyn, 'Contract Law: Fulfilling the Reasonable Expectations of Honest Men' (1997) 113 LQR 433, 439, educated in the Roman-Dutch system, has suggested that the House of Lords (or, now, the Supreme Court) might one day reconsider this point; Lord Neill QC, 'A Key to Lock-Out Agreements' (1992) 108 LQR 404, 410; Kötz, 'Towards a European Civil Code: The Duty of Good Faith', in P. Cane and J. Stapleton (eds.), *The Law of Obligations: Essays in Celebration of John Fleming* (Oxford, 1998), 244, 253 n. 30, cites other literature on this case.

29 [1992] 2 AC 128, HL.

The House of Lords held that an agreement to negotiate only with the other party would be valid, but only if restricted to a specified period. On this basis, a 'lock out' agreement for two weeks was upheld by the Court of Appeal in *Pitt v. PHH Asset Management Ltd* (1994)³⁰ (2.07).

In the absence of such a precise duration, the House of Lords in the *Walford* case held that the courts would not imply a term that the 'lock out' agreement would endure only for as long as would be reasonable. Such an implied term would require the court to decide whether it was fair or reasonable for the claimant to have withdrawn from the negotiations.³¹

The relevant passages in the speech by Lord Ackner are as follows:³²

The reason why an agreement to negotiate, like an agreement to agree, is unenforceable, is simply because it lacks the necessary certainty ... How can a court be expected to decide whether, subjectively, a proper reason existed for the termination of negotiations? The answer suggested depends upon whether the negotiations have been determined 'in good faith'. However the concept of a duty to carry on negotiations in good faith is inherently repugnant to the adversarial position of the parties when involved in negotiations. Each party to the negotiations is entitled to pursue his (or her) own interest, so long as he avoids making misrepresentations. To advance that interest he must be entitled, if he thinks it appropriate, to threaten to withdraw from further negotiations or to withdraw in fact, in the hope that the opposite party may seek to re-open the negotiations by offering him improved terms ...

A duty to negotiate in good faith is as unworkable in practice as it is inherently inconsistent with the position of a negotiating party. It is here that the uncertainty lies. In my judgment, while negotiations are in existence either party is entitled to withdraw from those negotiations, at any time and for any reason. There can be thus no obligation to continue to negotiate until there is a 'proper reason' to withdraw. Accordingly a bare agreement to negotiate has no legal content.

'Lock out' or 'exclusivity' agreement. Lord Ackner in *Walford v. Miles* (1992)³³ explained that parties can validly agree for consideration (in other words, for a price or something in return) that one or both will not negotiate with third parties (nor solicit offers, etc.), provided this period of 'exclusivity' is fixed:³⁴

There is clearly no reason in the English contract law why A, for good consideration, should not achieve an enforceable agreement whereby B agrees, for a specified period of time, not to negotiate with anyone except A in relation to the sale of his property. There are often good commercial reasons why A should desire to obtain such an agreement from B ... But I stress that this is a negative agreement – B by agreeing not to negotiate for this fixed period with a third party, locks himself out of such negotiations. He has in no legal sense locked himself into negotiations with A.

In *Pitt v. PHH Asset Management Ltd* (1994),³⁵ the Court of Appeal upheld a fixed-term 'lock out' agreement concerning negotiations for sale of property. The claimant and a third party

30 [1994] 1 WLR 327, CA.

31 *Walford v. Miles* [1992] 2 AC 128, 140, HL.

32 *Ibid.*, at 138.

33 *Ibid.*

34 *Ibid.*, at 139–40.

35 [1994] 1 WLR 327, CA.

were in a 'property race'. The 'lock out' agreement gave the claimant the benefit of a fourteen-day period of exclusive dealing with the defendant. This 'lock out' proposal was made in a letter from the claimant, which the defendant confirmed by letter. In fact, the defendant later sold the property to a third party because the claimant could not beat the third party's offer. This rival offer had been accepted by the defendant within the period of the 'lock out' agreement. Following *Walford v. Miles* (see above), the Court of Appeal in the *Pitt* case recognised that a 'lock out' agreement is not uncertain, provided its duration is fixed. Secondly, the Court of Appeal held that there was no need for compliance with the strict formalities of the Law of Property (Miscellaneous Provisions) Act 1989 requiring joint signature and inclusion of all the terms in a single document (5.07); in short, a 'lock out' arrangement does not fall within the notion of an agreement for sale of an interest in land within section 2 of that Act. Nor was the 'lock out' agreement 'subject to contract', unlike the main contract (on 'subject to contract', see 6.06, 1.16, 2.07, 4.21, 12.04). Finally, there was consideration (on which, generally, see chapter 5) supplied by the claimant: (1) that party's withdrawal of a complaint; and (2) the defendant's receipt of a probable benefit in gaining a speedy conclusion of the main deal. And so the Court of Appeal, upholding the first instance judge, ordered damages to be assessed for breach of the 'lock out' agreement.

- 2.08 *Agreement to use best or reasonable endeavours to reach agreement on main aspect(s) of the proposed transaction.* As noted above (2.07), the House of Lords in *Walford v. Miles* (1992)³⁶ held that an agreement to negotiate *in good faith* is void for uncertainty. Similarly, English law will not give effect to an undertaking *to use best or reasonable endeavours to reach agreement on the main parts of the proposed deal*, for example, dealings designed to clarify the nature of the subject matter or to fix the price. In *Little v. Courage* (1995), Millett LJ explained this approach: 'an undertaking to use one's best endeavours to agree ... is no different from an undertaking to agree, to try to agree, or to negotiate with a view to reaching an agreement; all are equally uncertain and incapable of giving rise to an enforceable obligation.'³⁷ The Court of Appeal endorsed this statement in *London & Regional Investments Ltd v. TBI plc* (2002).³⁸ (Here, English law differs from New York law, as the English Court of Appeal in *AT&T Corporation v. Saudi Cable Co.* (2000)³⁹ noted.) *Little v. Courage* is difficult, although not perhaps impossible (see factors (1) to (3) below), to reconcile with the Privy Council decision in *Queensland Electricity Generating Board v. New Hope Collieries* (1989).⁴⁰ As Lord Neill observed (1992),⁴¹ the Privy Council in the *Queensland* case upheld a 'reasonable endeavours' negotiation clause. The court's judgment was given by Sir Robin Cooke (the other judges were Lords Diplock, Fraser, Roskill and Brightman). As Neill (in his journal article) explains:⁴²

36 [1992] 2 AC 128, HL.

37 (1995) 70 P & CR 469, 476, CA.

38 [2002] EWCA Civ 355, at [39] and [40].

39 [2000] 2 Lloyd's Rep 127, at [3] and [4].

40 [1989] 1 Lloyd's Rep 205, PC.

41 (1992) 108 LQR 405, 407–8.

42 *Ibid.*

The *Queensland* case concerned a 15-year supply contract whereby the Colliery Company agreed to supply coal to the Generating Board. For the first five-year period the contract contained a scale of base prices and elaborate 'escalation' or 'price variation' provisions for adjusting the base prices for changes in the company's costs. For purchases after the first five years the general terms of the agreement were to continue. It was stipulated: 'The base price and provisions for variations in prices ... shall be agreed by the parties ...'. There was a comprehensive arbitration clause. The Generating Board contended (inter alia) that for the period after the first five years the agreement was uncertain and constituted nothing more than an agreement to agree. The Privy Council rejected this plea.

Three aspects of this case are noteworthy: (1) the negotiation clause applied to a renewal of a commercial contract, which had already run for five years; (2) Sir Robin Cooke emphasised⁴³ that the arrangement was subject to a widely drafted arbitration clause, so that in default of agreement there was a safety net; (3) Sir Robin Cooke expressly distinguished between a 'subjective' determination of fairness by the arbitrator (something which would be unacceptably uncertain) and the arbitrator's capacity in this context to reach an 'objectively fair and reasonable' determination, based upon admittedly 'broad' factors (the words in quotation are Sir Robin Cooke's, rather than those of the contractual clause). Without articulating these three points, Potter LJ in *Phillips v. Enron* (1997) clearly stated⁴⁴ that he was content that the *Queensland* case involved application of an objective set of criteria (see further 4.03).

2.09 Criticism of the Walford case. Berg, writing in the *Law Quarterly Review* (2003), has suggested a radically new approach:⁴⁵ even where the main contract has not yet been formed, an agreement to negotiate in good faith should validly impose various implied negotiation duties.

Berg proposes as follows:

An undertaking to negotiate 'in good faith' is to be construed as an agreement to renounce purely adversarial negotiation. Subject to the particular factual setting, such an undertaking can be taken to involve: (1) an obligation to commence negotiations and to have some minimum participation in them; compare *Cable & Wireless plc v. IBM United Kingdom Ltd* (2002),⁴⁶ where the contract required the parties to go thorough a clearly defined mediation procedure.

My objection to Berg's proposition is as follows. Obligation (1) is misleading, and Berg has overstated the content of the 'contractual obligation to pursue mediation'. The current law satisfactorily distinguishes (a) a 'no show', that is, an absolute refusal to consider

⁴³ [1989] 1 Lloyd's Rep 205, 210, PC.

⁴⁴ [1997] CLC 329, 343, CA; also, at 339, explaining *Queensland Electricity Generating Board v. New Hope Collieries* [1989] 1 Lloyd's Rep 205, PC, on this basis.

⁴⁵ (2003) 110 LQR 357.

⁴⁶ [2002] EWHC 2059; [2002] 2 All ER (Comm) 1041.

mediation and (b) alleged unreasonable conduct of the mediation process. Complaints of type (b) do not involve contractual wrongdoing. But a complaint concerning 'stonewalling' at stage (a) does, as the *Cable & Wireless* case (2002) (2.13) shows. In that case, Colman J accepted that parties should not proceed to formal litigation if they have agreed that they will first attempt to settle their dispute before a neutral mediator. He ordered a 'stay' of the premature court litigation. This suspension of court proceedings would permit the parties to resort to mediation, as they had agreed. If mediation did not work, the court proceedings would resume: the 'stay' would be lifted. It should be noted, however, that the *Cable & Wireless* case does not *legally require* negotiating parties to meet and to discuss a dispute or to participate in mediation. How would damages be assessed? An injunction to compel such a duty is unthinkable. Furthermore, the English courts will not scrutinise the parties' conduct before a mediator (unless both parties waive the evidential privilege attaching to those negotiations, 2.14).

Berg further proposes that a promise to negotiate in good faith will also impose:

(2) an obligation to have an open mind [during negotiations] in the sense of: (i) a willingness to consider such options for the resolution of the dispute as may be proposed by the other party, (ii) a willingness to give consideration to putting forward options for the resolution of the dispute;⁴⁷

(3) an obligation not to take advantage, in the course of the negotiations, of the known ignorance of the other party ... and

(4) (A) an obligation not to withdraw from the negotiations without first giving a reason and a reasonable opportunity for the other party to respond; (B) not to withdraw giving a reason which is untrue (e.g., 'I have received a higher offer', when none has been received); and (C) not to withdraw giving as the cause something which the withdrawing party knows is extremely unreasonable (in approximately the *Wednesbury* sense),⁴⁸ such as the other party's failure to agree to a request which the withdrawing party knows that the other party could not reasonably be expected to have accepted.

My objection to this is that obligation (2) is unacceptably vague; and it is doubtful whether an agreement to impose such an obligation would be commercially attractive. Obligations (3), and (4) (A) and (C), even if contained in an express clause, would unacceptably fetter the process of bargaining and would produce difficult and protracted disputes. Obligation (3) is clearly not English law (3.66 ff). Even objection (4) (B), a duty to refrain from giving a deliberately false reason for quitting a negotiation, is troublesome. It is a pervasive and innocuous feature of business negotiation that one side will 'gently let down the other' by giving a pretext for not proceeding with the negotiations. To outlaw such 'white lies' and

47 Berg adds this reference: *Aiton Australia Pty Ltd v. Transfield Pty Ltd* [1999] NSWSC 996, at [147] to [156].

48 Berg is alluding to the principles of judicial review of administrative decisions founded upon *Associated Provincial Picture Houses v. Wednesbury Corporation* [1948] 1 KB 223, CA, per Lord Greene MR.

‘face-saving’ untruths would be out of step with commercial practice and hence naïve. Berg’s suggestions seem unsuitable for use within the rough-and-tumble of commercial dealings. Nor should it matter that the parties have freely undertaken to ‘negotiate in good faith’, thus triggering Berg’s cascade of obligations. There are limits to the principle of freedom of contract (1.08). That principle does not justify the courts straying into the commercial minefield of negotiations conducted in a tough and bullish manner. Berg’s criteria would transport English courts into this danger zone. His suggested criteria lie beyond the boundary of practical common sense. They provide no satisfactory criteria for public adjudication by the courts or arbitrators.

4. AGREEMENTS ANCILLARY TO A SETTLED AGREEMENT

- 2.10 *Agreement to use reasonable or best endeavours to obtain an official permission.* The *Walford* case (1992)⁴⁹ and *Little v. Courage* (1995)⁵⁰ acknowledge as settled law⁵¹ the validity of an agreement to use ‘best’, ‘all reasonable endeavours’ or ‘reasonable endeavours’ to obtain planning permission, or an export licence, or to procure a third party’s consent. Such an undertaking is sufficiently clear and restricted. Its recognition does not fetter the parties’ freedom to negotiate. It is an obligation to try to procure a specific external consent necessary for the achievement of the main transaction: in other words, to try to unlock the door controlled by a third party. It is not an absolute commitment, or guarantee of success.

A thesaurus of graduated obligations is emerging. Obligations to exercise ‘*best endeavours*’ or ‘*all reasonable endeavours*’ are more onerous than an undertaking to exercise ‘*reasonable endeavours*’ (although ‘all reasonable endeavours’ might be similar to ‘best endeavours’). As Judge Julian Flaux QC said in the *Rhodia* case (2007):⁵² ‘An obligation to use *reasonable endeavours* to achieve the aim probably only requires a party to take one reasonable course, not all of them, whereas an obligation to use *best endeavours* probably requires a party to take all the reasonable courses he can. In that context, it may well be that an obligation to use *all reasonable endeavours* equates with using *best endeavours*’ (but see the qualification in the text at (c) below).

In a *dictum* (see point (1) immediately below), Vos J in the ‘Chelsea Barracks case’ (2010) suggested, first, that ‘the obligation to use “all reasonable endeavours” does not always require the obligor to sacrifice his commercial interests’. Secondly, he added: ‘In

49 [1992] 2 AC 128, at 139–40, HL.

50 (1995) 70 P & CR 469, 476, CA.

51 Other authorities: *P&O Property Holdings Ltd v. Norwich Union Life Insurance Society* (1994) 68 P & CR 261, HL; *Phillips Petroleum Co. UK Ltd v. Enron Europe Ltd* [1997] CLC 329, CA; *Rae Lambert v. HTV Cymru (Wales) Ltd* [1998] FSR 874, CA; and see the cases cited in the next note.

52 *Rhodia International Holdings Ltd v. Huntsman International LLC* [2007] EWHC 292 (Comm); [2007] 2 Lloyd’s Rep 325, at [33] ff (noted by B. Holland, (2007) 18 *International Company and Commercial Law Review* 349); also examining *Yewbelle Ltd v. London Green Developments Ltd* [2006] EWHC 3166 (Ch) (Lewison J), at [118] ff; Lewison J’s analysis was considered in the *Yewbelle* case on appeal, [2007] EWCA Civ 475; [2008] 1 P & CR 17, at [29] ff by Lloyd LJ; and these remarks were applied by Vos J in *CPC Group Ltd v. Qatari Diar Real Estate Investment Company* [2010] EWHC 1535; [2010] NPC 74, at [249] ff (the ‘Chelsea Barracks case’).

this case, the matter is, however, clearer because the contract itself ... contains other indications that [the defendant] was not to be required to sacrifice its commercial interests. Indeed the words of clause 7.1 itself make that clear by using the added words “but commercially prudent” in the phrase “all reasonable but commercially prudent endeavours”⁵³

Furthermore, Vos J held that an obligation to use ‘all reasonable but commercially prudent endeavours’ in obtaining planning permission (1) does not require a party ‘to ignore or forgo its commercial interests’, but (2) requires that party ‘to take all reasonable steps to procure the Planning Permission, provided those steps are commercially prudent’; and he added (3) that an obligation to use ‘all reasonable but commercially prudent endeavours’ is ‘not equivalent to a “best endeavours” obligation’.⁵⁴

- 2.11 *Post-formation negotiation agreements.* If the main contract already subsists, Longmore LJ has suggested, in reasoned *dicta* in *Petromec Inc. v. Petroleo Brasileiro SA* (2005),⁵⁵ that a ‘bolt-on negotiation clause’ *might* be valid, and that the *Walford* case (1992)⁵⁶ (2.07) should not preclude these. This is a workable and valuable gloss to the *Walford* case if (and only if) the court can discern an *objective and clear criterion* to determine whether the obligation has been breached. Longmore LJ’s stimulating *dicta* will now be explored in detail.

The Court of Appeal’s 2005 decision in the *Petromec* case was part of a long chain of complicated litigation. The main contract was a complex arrangement concerning the purchase, upgrading and hire of an oil rig. The relevant negotiation clause stated: ‘Clause 12.4: Brasoil agrees to negotiate in good faith with Petromec the extra costs referred to in clause 12.1 and 12.2 above and the extra time referred to in clause 12.2 above.’ The actual decision was that this clause did not apply to the dispute during performance. And so the status of this clause did not arise for decision.

However, Longmore LJ in the *Petromec* case indicated that the clause might otherwise have been valid. He suggested that there are three objections to an agreement to negotiate in good faith: (1) *uncertainty* (‘the obligation is an agreement to agree and thus too uncertain to enforce’); (2) *the contestable nature of bad faith* (‘it is difficult, if not impossible, to say whether, if negotiations are brought to an end, the termination is brought about in good or in bad faith’); and (3) *difficulty in assessing loss* (‘since it can never be known whether good faith negotiations would have produced an agreement at all or what the terms of any agreement would have been if it would have been reached, it is

53 *CPC Group Ltd v. Qatari Diar Real Estate Investment Company* [2010] EWHC 1535; [2010] NPC 74, at [252].

54 *Ibid.*, at [253].

55 [2005] EWCA Civ 891; [2006] 1 Lloyd’s Rep 121, at [115] (Longmore LJ acknowledging that comments are *dicta*); on which see M. Chen-Wishart, *Contract Law* (2nd edn, Oxford, 2007), 105 ff; E. McKendrick, ‘The Meaning of Good Faith’, in *Liber Amicorum Guido Alpa: National Private Law Systems* (London, 2007), 687.

56 [1992] 2 AC 128, at 139–40, HL.

impossible to assess any loss caused by breach of the obligation’).⁵⁷ He then suggested that objections (1) and (3) are *irrelevant* if the negotiation clause arises out of a *valid agreement*. Objection (1) falls away because there is a main contract and so the ‘agreement to agree’ problem vanishes. And objection (3) would not be a problem because the court could work out adequate compensation for the amount which might by reasonable negotiation have become payable by one party to the other.⁵⁸ As for objection (2) (the question of good or bad faith), Longmore LJ suggested that, in the present *post-formation* context (that is, a negotiation clause *ancillary to the main contract*), the notion of ‘bad faith’ would not prove problematic. More generally, he suggested that the law should not shy away from upholding a duty to negotiate in good faith where it is part of a subsisting agreement and the parties have inserted it in the confident belief that it would create a workable framework for fixing their entitlements under the main contract.

The upshot of these *dicta* is that the Court of Appeal or the Supreme Court *might* (the point has yet to be settled by an authoritative decision) distinguish the decision in *Walford v. Miles* (1992)⁵⁹ so that it only invalidates a good faith negotiation obligation if it concerned the establishment of the main agreement, as distinct from an ancillary negotiation clause ‘tacked onto a subsisting agreement’. An ancillary negotiation obligation will be upheld if:

- (1) it was express (although *Chitty on Contracts* (2008) contends that a court might imply a term to negotiate on outstanding, presumably minor, details if the main parts of a contract are established and those parts are intended to be binding);⁶⁰
- (2) the parties have not reserved to themselves the task of reaching final consensus on the matter to be negotiated;
- (3) the parties have employed *criteria which are clear enough to permit the courts to determine the matter themselves, without guessing at a fair result*; as mentioned at 4.08 and 4.09, the Court of Appeal in *Didymi Corporation v. Atlantic Lines* (1988)⁶¹ upheld a hire variation clause designed to reflect the ship’s speed and efficiency; adjustment should be ‘agreed’ according to what was ‘equitable’; the contract had already lasted for a significant period before the disputed issue arose; although the *Didymi* decision upholds the word ‘equitable’ in that particular commercial context (efficiency of a chartered vessel’s sailing performance), the same word might not possess sufficient certainty in all other contexts; in *Phillips Petroleum Co. (UK) Ltd v. Enron (Europe) Ltd* (1999), which concerned a commercial undertaking to exercise reasonable endeavours to negotiate terms within an existing agreement, Potter LJ approved the *Didymi* case’s emphasis upon reliable and objective criteria;⁶² but, in

57 [2005] EWCA Civ 891; [2006] 1 Lloyd’s Rep 121, at [116].

58 *Ibid.*, at [117] and [118].

59 [1992] 2 AC 128, at 139–40, HL.

60 *Chitty on Contracts* (30th edn, London, 2008), 2-138 (citing *Donwin Productions Ltd v. EMI Films Ltd*, 9 March 1984 (Peter Pain J); decision not followed in the context of incomplete compromise in *Dalgety Foods Holland BV v. Deb-its Ltd* [1994] FSR 125, Nugee QC; and *Donwin* case not cited in *Walford v. Miles* [1992] 2 AC 128, HL).

61 [1988] 2 Lloyd’s Rep 108, CA; noted by Reynolds, (1988) 104 LQR 353.

62 [1996] EWCA Civ 693; [1997] CLC 329, 343–4, *per* Potter LJ, where he noted that, in *Didymi Corporation v. Atlantic Lines* [1988] 2 Lloyd’s Rep 108, CA (noted by Reynolds, (1988) 104 LQR 353) (4.08 and 4.09),

the *Phillips* case, the court there held that the negotiation clauses lacked objective criteria and none could be convincingly or reliably implied; and Toulson LJ made a similar point, sitting at first instance, in *BBC Worldwide Ltd v. Bee Load Ltd* (2007).⁶³

- 2.12 *Post-formation obligation to observe 'utmost good faith'*. In *Berkeley Community Villages Ltd v. Pullen* (2007), Morgan J held that, *once a contract has been formed*, the law will recognise as valid a clause which *expressly imposes a duty of 'utmost good faith' on the parties during performance*.⁶⁴ The notion of 'good faith' is not uncertain if it is linked to (1) a *performance* obligation as distinct from (2) a *negotiation* obligation. If 'good faith' is linked to (1), it will impose a positive duty to take action consistent with the achievement of the contract's main purpose; and it will impose a negative duty to refrain from conduct which will stultify that purpose (see the further discussion of the 'Chelsea Barracks' case (2010) below).

In the *Berkeley Community Villages* case (2007), landowner P and consultant B had agreed to develop P's property. B was to obtain planning permission. B would then gain a commission. B incurred considerable sums attempting to gain this planning permission (these were not steps taken at its own risk; the whole matter was *not* 'subject to contract'; compare the *Cobbe* case (2008), discussed at 5.66 case (2)). Before this permission had been formally obtained, P proposed to sell part of the land to a third party. That would deprive B of his right to commission. The relevant clause (clause 33) in this development contract stated: 'the parties will act with the utmost good faith towards one another and will act reasonably and prudently at all times.' Morgan J held that this clause validly imposed 'on the Defendants a contractual obligation to observe reasonable commercial standards of fair dealing and ... faithfulness to the agreed common purpose'.⁶⁵ He granted an injunction to prevent P from selling the land to a third party until B had gained the right to a commission (that is, after planning permission had been finalised in favour of P).

In the 'Chelsea Barracks' case (2010),⁶⁶ Vos J, after considering the *Berkeley Homes* case (2007) and related decisions, noted that the obligation in the present case was that the parties to a development agreement 'shall both act in the utmost good faith towards each

Nourse and Dillon LJ had given effect to the word 'equitable' because (in Potter LJ's words) it disclosed 'a standard of fairness and reasonableness', that is, 'an objective criterion to which the court is frequently willing to resort when determining a price or other sum not specifically agreed but readily assessable by reference to market rates and prices in the relevant sphere'; but, in the *Phillips* case, 'no such straightforward or well-established exercise arises in a "one-off" case of this kind in which no criteria have been specified and there are a variety of considerations which may legitimately operate in the minds of the parties in relation to their ability or willingness to agree upon a specific date' during a North Sea oil project.

63 [2007] EWHC 134 (Comm), at [93] and [95] (Westlaw report).

64 [2007] EWHC 1330 (Ch); [2007] 3 EGLR 101; [2007] 24 EG 169 (CS); [2007] NPC 71, Morgan J.

65 *Ibid.*, at [97].

66 *CPC Group Ltd v. Qatari Diar Real Estate Investment Company* [2010] EWHC 1535; [2010] NPC 74, at [237] ff.

other'. Vos J held⁶⁷ that this imposed a duty 'to adhere to the spirit of the contract, which was to seek to obtain planning consent for the maximum Developable Area in the shortest possible time, and to observe reasonable commercial standards of fair dealing, and to be faithful to the agreed common purpose, and to act consistently with the justified expectations of the parties'. And he added: 'I do not need, it seems to me, to decide whether this obligation could *only* be broken if [the parties] acted in bad faith, but it might be hard to understand ... how, without bad faith, there can be a breach of a "duty of good faith, utmost or otherwise"'.

5. MEDIATION AGREEMENTS⁶⁸

- 2.13 Mediation agreements normally arise out of a pre-existing relationship, especially contractual relations. Mediation clauses (often part of a more complex multi-level dispute clause: see the next paragraph) are now a common feature of commercial contracts. As Colman J decided in *Cable & Wireless plc v. IBM United Kingdom Ltd* (2002),⁶⁹ the courts will 'stay' (that is, place in suspense) formal proceedings until the stipulated prior mediation process has been properly considered. The innocent party can validly complain that the other party should not have bypassed the contractually obligatory mediation phase (although exceptionally this might be excused: see the case discussed below). It is of relevance that the English procedural rules (the CPR) emphasise generally the civil courts' responsibility to promote alternative dispute resolution.⁷⁰

In *Cable & Wireless plc v. IBM United Kingdom Ltd* (2002),⁷¹ IBM had agreed to supply long-term IT services to Cable & Wireless. The contract contained a multi-level dispute-resolution clause. It provided that, if a dispute arose concerning the adequacy of IBM's performance, the parties would first try to settle the matter in good faith among themselves. If the dispute remained unsettled, they agreed to take it to a higher level of management, again among themselves. If that did not work, they agreed to refer it to mediation before an external and named commercial mediator. If that failed, it was agreed that they would litigate. But Cable & Wireless skipped the mediation phase and went straight to the High Court. The substantive claim was for £45m damages. Colman J upheld IBM's complaint that Cable & Wireless' commencement of High Court litigation was premature and a breach of the dispute-resolution clause. Cable & Wireless should not have leap-frogged the mediation. To remedy this, Colman J ordered a 'stay' of the High Court proceedings. This was to enable the parties to pursue mediation. Only if that failed would the High Court case be reactivated, whereupon the stay would be lifted.

67 [2010] EWHC 1535; [2010] NPC 74, at [246].

68 On connections between civil proceedings, mediation, settlement and arbitration, see N. Andrews, *The Modern Civil Process* (Tübingen, 2008).

69 *Cable & Wireless plc v. IBM United Kingdom Ltd* [2002] 2 All ER (Comm) 1041.

70 CPR 1998, Rule 1.4(2)(e); generally on the interplay between civil proceedings, mediation, settlement and arbitration, see N. Andrews, *The Modern Civil Process* (Tübingen, 2008).

71 *Cable & Wireless plc v. IBM United Kingdom Ltd* [2002] 2 All ER (Comm) 1041.

- 2.14 However, the English courts will not scrutinise the parties' conduct during a mediation hearing. Not only would such a judicial examination be difficult, but mediation discussions are also confidential and privileged. This means that no evidence can be adduced of what was said or written by the parties during the course of mediation discussions, unless both parties' permission is obtained to use such evidence. It is different if there has been a joint waiver of this evidential rule. And so Jack J in *Carleton v. Strutt & Parker* (2008) said that the courts will consider the 'unreasonableness' of positions taken in the mediation if *the parties have waived privilege in their mediation communications*, and the question concerns assessment of costs in litigation subsequent to an unsuccessful mediation.⁷²
- 2.15 Sometimes the parties might insert a clause requiring 'expert determination', for example the valuation of shares by a neutral third party auditor. The expert's decision is binding on the parties, but the process takes place outside the Arbitration Act 1996. Clark J in *Thames Valley Power Ltd v. Total Gas & Power Ltd* (2005) held that the court might stay English court proceedings if they would involve a failure to adhere to an undertaking to refer the matter to 'expert determination'.⁷³ But on the facts of this case he exercised his discretion by deciding not to award a 'stay' because of the need for speed and also because he could see no substantive merit in the defaulting party's case.

72 [2008] EWHC 424; 118 Con LR 68; [2008] 5 Costs LR 736; (2008) 105(15) LSG 24; (2008) 158 NLJ 480, at [72]; J. Sorabji, (2008) 27 *Civil Justice Quarterly* 288, 291–2.

73 [2005] EWHC 2208 (Comm); [2006] 1 Lloyd's Rep 441, at [6], for the terms of the relevant *force majeure* clause.

Chapter contents

1. Introduction *para. 3.01*
2. 'Invitations to treat' and 'offers' distinguished *para. 3.02*
3. The process of offer and acceptance in general *para. 3.05*
4. Postal acceptances *para. 3.18*
5. Counter-offers *para. 3.29*
6. Battle of the forms *para. 3.32*
7. Revocation and termination of offers *para. 3.35*
8. Acceptance in the context of unilateral contracts *para. 3.40*
9. Auctions, tenders and fixed bid competitions *para. 3.47*
10. The objective principle of consent *para. 3.57*

3

Offer and acceptance

1. INTRODUCTION¹

3.01 Summary of main points

This chapter concerns the process of reaching a consensus. Here the analysis is dominated by 'offer and acceptance'. The main points of discussion will be:

The process of offer and acceptance

- (1) In many situations, especially when the parties are in correspondence, English law requires an agreement to result from acceptance of an offer; however, it is admitted that some situations produce a consensus without such a clear-cut form of dealing.
- (2) An offer can be made to an individual, a member of a group, or even the public at large; acceptance presupposes knowledge of an offer; acceptance must be made by an intended offeree; the general rule is that contracts involving reciprocal obligations ('bilateral contracts') cannot be accepted by silence; but sometimes an agreement can arise if the offeree has acted on the offer in a manner indicating implied assent to it ('acceptance by conduct').
- (3) Offers should be distinguished from a mere 'invitation to treat'; such an invitation is an opportunity for further dealings, but not a communication or presentation rendering the relevant party's goods (or services etc.) open to immediate acceptance; for example, goods on display in shops are not available to be immediately accepted; and most advertisements for goods or services are regarded as 'invitations to treat'.
- (4) An offeree can make a counter-offer; if this is rejected, and the original offer is not reinstated, the offeree cannot accept the original offer.

¹ On the nineteenth-century history of this topic, see M. Lobban, in W. Cornish, J. S. Anderson, R. Cocks, M. Lobban, P. Polden and K. Smith, *The Oxford History of the Laws of England*, vol. XII, 1820–1914: *Private Law* (Oxford, 2010), 329 ff.

- (5) An offeree cannot validly accept an offer if the offeror has directly revoked it by successfully communicating a cancellation of the offer; nor can the offeree validly accept if he has indirectly acquired knowledge that the offer is no longer open to acceptance by him.
- (6) A statement (other than a binding option made for consideration or presented formally as a deed) that an offer is open to acceptance for a specified period can be revoked, directly or indirectly, within the stated period; such revocation, reaching the offeree either directly or indirectly, will preclude valid acceptance unless the offeree has already accepted (for the rule that acceptance by post normally occurs upon posting, see (8) below).
- (7) If it is reasonable to send an acceptance by post, and provided the offeror has not expressly required receipt of the acceptance, the English 'postal rule' fixes a valid agreement at the moment of posting; when the postal rule applies, acceptance is complete upon posting, even if the letter is delayed by the postal service (for reasons other than the offeree's fault) and even if the letter is lost in the post; however, it appears that the postal rule will not apply to circumstances where it would involve 'manifest inconvenience' or 'absurdity'; this restriction might be interpreted to apply whenever a deadline for response has been specified, for example, notification of the intention to exercise an option by a specified date.
- (8) English law applies strictly the offer and acceptance analysis even if negotiations involve competing and discordant standard terms; the 'battle of forms' is won by the party whose offer is eventually accepted by the opponent; other approaches to this problem might be suggested, but these have not been adopted in England.

Particular contexts

- (9) An 'invitor' requesting tenders does not normally commit himself to award a tender, but he must at least consider valid tenders, disregard invalid tenders, refrain from making a final decision before a specified deadline has passed, and generally adhere to the specified terms of his tendering process.
- (10) If there is no reserve price (or where the bid exceeds the reserve price), an auctioneer who refuses to 'knock down' in favour of the highest bidder is in breach of a collateral contract (even though there is no contract of sale between the owner and the bidder).
- (11) An offeror can commit himself to accept the highest or best bid, for example, by issuing invitations for interested persons to send 'sealed bids' to purchase property; each bid must normally be for a fixed and free-standing amount; the law invalidates a 'referential bid' designed to top the other's (as yet unascertained) fixed bid by a specified sum (at any rate if a referential bid, subject to an overall financial 'cap', has not been expressly requested from each competitor).

Unilateral contracts

- (12) In the case of a unilateral contract, it is normal to regard the offeror as having 'waived the need for express acceptance'; the promisor becomes fully obliged to honour his commitment if the requested act has been fully performed; however, in some situations (but not in all), protection of the offeree's reliance and expectations requires that the offeror should lose his power to revoke the offer pending complete performance by the offeree; the better view is that such protection, where it is appropriate, is based on the implication of a collateral contract.

The objective principle

- (13) The parties' language and conduct must be assessed according to their apparent and reasonable meaning and appearance; this is the 'objective principle of consensus'.
- (14) If party B knows that party A has made an apparent offer in error, or that A has presented the terms of the offer erroneously (for example, the price), B cannot take advantage of A's error; similarly, short of proof of actual knowledge, it might be enough that B ought reasonably to have realised that A has made such an error; however, where B knows that A is mistaken concerning the quality of the relevant subject matter, or its unwarranted value, the law does not object to B taking advantage of A's error, even though this might be regarded as morally 'shabby'; however, in this last situation, it is different if B knows that A believes that there is a tacit warranty that the subject matter should possess the relevant quality or value (the rule in *Smith v. Hughes*, 1871); and it is possibly the law that A can then insist on enforcing the bargain on A's supposed terms.

M. Furmston and G. J. Tolhurst, *Contract Formation: Law and Practice* (Oxford, 2010) (rich in Commonwealth and American discussion), notably chapters 2–4

S. Gardner, 'Trashing with Trollope: A Deconstruction of the Postal Rules in Contract' (1992) 12 OJLS 170, especially 192 to end

A. H. Hudson, 'Retraction of Letters of Acceptance' (1966) 82 LQR 169–73

E. McKendrick, 'The Battle of the Forms and the Law of Restitution' (1988) 8 OJLS 197, especially 215–18, 220–1

E. McKendrick, *Contract Law: Text, Cases and Materials* (4th edn, Oxford, 2010), 92–3

2. 'INVITATIONS TO TREAT' AND 'OFFERS' DISTINGUISHED²

- 3.02 An offer is a clear expression of an unequivocal willingness to be bound upon the offer-ee's acceptance (an acceptance is an unequivocal expression of willingness to accede,

2 M. Furmston and G. J. Tolhurst, *Contract Formation: Law and Practice* (Oxford, 2010), chapter 2. On the test for ascertaining whether a communication discloses an offer, *Crest Nicholson v. Akaria* [2010] EWCA civ 1331, at [25].

without significant qualification, to the terms contained in the offer). An offer can be made to an ascertained individual, to two or more persons, or even to the world at large. Offers must be contrasted with preliminary communications not intended to be open to acceptance, namely, ‘invitations to treat’ (on which see 3.03). Only an intended offeree can accept an offer, and not an unauthorised busybody.³ Normally, it will be safe to assume that the word ‘offer’ can be taken at face value. But sometimes the word ‘offer’ is used inaccurately in casual language, even in commercial contexts,⁴ when in fact the relevant communication is merely a preliminary statement not intended to create the possibility of immediate acceptance.

- 3.03 *Invitations to treat (1): advertisements.*** The general rule is that an advertisement of goods or services is *prima facie* an ‘invitation to treat’ and *not an offer*. This is supported by various decisions, notably *Grainger & Sons v. Gough* (1896) and *Partridge v. Crittenden* (1968).⁵ Therefore, the advertiser is not subject to immediate demands for acceptance. He can decide whether to accept the responding public’s requests for delivery. The rationale for this presumption is that the advertiser might otherwise be exposed to a torrent of demands. As Lord Herschell said in the *Grainger* case (1896): ‘the merchant might find himself involved in any number of contractual obligations to supply [goods] of a particular description which he would be quite unable to carry out, his stock ... being necessarily limited.’⁶ However, this rationale is not quite convincing because it would be easy to imply the qualification that the offer applies ‘while stocks last’. Therefore, a better approach would be to treat a *clear-cut expression of willingness to be bound*, even if contained in an advertisement, as open to acceptance, either, where there is only one item, on the implicit basis ‘first come, first served’ or, where a series of sales is contemplated, on the implicit basis ‘while stocks last’.

The restrictive approach of English law to this matter can be contrasted with a leading decision in the USA, where a *clear-cut* advertisement of (non-hazardous) goods at a store has been held to be capable of acceptance, the store-owner having no further opportunity to quibble:

In the American decision in *Lefkowitz v. Great Minneapolis Surplus Stores* (1957), a newspaper advertisement stated that the defendant store was willing to sell a fur stole ‘worth \$139.50 for \$1.00, first come, first served’. It was held that this left nothing for further negotiation. The defendant’s refusal to sell to the claimant was a breach of contract, and it was liable for damages to compensate for the claimant’s loss of bargain, \$138.50. However, other items were not subject to the same analysis. This was because their real value had not been clearly disclosed in the advertisement: ‘3 brand new coats worth up to \$100’.⁷

3 *Boulton v. Jones* (1857) 27 LJ Ex 117: 10.40.

4 E.g. *Datec Electronics Holdings Ltd v. United Parcels Services Ltd* [2007] UKHL 23; [2007] 1 WLR 1325; *Chitty on Contracts* (30th edn, London, 2008), 2-009.

5 *Grainger & Sons v. Gough* [1896] AC 325, HL; *Partridge v. Crittenden* [1968] 1 WLR 1204, Divisional Court.

6 *Grainger & Sons v. Gough* [1896] AC 325, 334, HL.

7 86 NW 2d 689 (1957) (Sup Court of Minnesota).

Treitel also suggests that (in England) a supplier's list of goods sent *on request* to a possible customer might be treated as a definitive set of offers, because the supplier would be implying that he has adequate supplies.⁸

As for *unilateral contracts*, *Carlill v. Carbolic Smoke Ball Co.* (1893)⁹ (3.42) shows that there is a true offer, not a mere *invitation to treat*, if an advertisement contains an unequivocal offer of a reward. This statement is intended to spur readers into action. In law it is intended to create a unilateral contract. There can be only one, or at least a limited number of, successful offerees. No haggling is contemplated.

- 3.04 *Invitations to treat (2): goods on display.*¹⁰ The rule is that goods displayed in a shop are not available for immediate acceptance. Such a display is regarded as an 'invitation to treat', that is, a preliminary stage without the possibility of immediate binding acceptance. This means that the customer's attempt to buy the goods is at best an offer: she cannot immediately accept. In stores where customers are allowed to roam the shelves (a modern pastime), placing items in baskets or trolleys, and then proceeding to pay, an offer is made by the customer when she takes the goods to the cash desk. The proprietor and staff can refuse to accept that offer. In principle, the shop-owner can refuse to sell even for quite capricious or odd reasons, for example, membership of the wrong university, or support for the wrong football team (but it would be legally unacceptable to do so on grounds of gender,¹¹ racial group¹² or disability¹³). Indeed, in some situations, it will be an offence for the proprietor to sell controlled or prohibited substances: persons under age wishing to purchase alcohol,¹⁴ tobacco (and cigarette papers),¹⁵ fireworks,¹⁶ gunpowder,¹⁷ knives and axes;¹⁸ adults wishing to buy methylated spirits for consumption,¹⁹ poisons (and various glues),²⁰ flick knives,²¹ machine guns, and mortar-launchers and other missile-launchers.²²

⁸ *Treitel* (12th edn, London, 2007), 2-010 n. 62.

⁹ [1893] 1 QB 256, CA.

¹⁰ *Fisher v. Bell* [1961] 1 QB 394, Divisional Court; and, especially, *Pharmaceutical Society of Great Britain v. Boots etc. Ltd* [1953] 1 QB 401, CA.

¹¹ Section 6(1)(c) of the Sex Discrimination Act 1975.

¹² Sections 4(1)(c), 17, 20 and 21 of the Race Relations Act 1976; cf *Timothy v. Simpson* (1834) 6 C & P 499; 172 ER 1337; (1835) 1 CM & R 757; 149 ER 1285 (shopkeeper's anti-semitic refusal to serve a Jew at listed price; attempt to raise ticketed price on the spot; altercation; affray; arrest; allegation of false imprisonment).

¹³ Disability Discrimination Act 2005; Disability Discrimination Act (Amendment) Regulations 2003 (SI 2003 No. 1673).

¹⁴ Section 146 of the Licensing Act 2006.

¹⁵ Section 7 of the Children and Young Persons Act 1933.

¹⁶ Section 3 of the Fireworks Act 2003.

¹⁷ Section 31 of the Explosives Act 1875.

¹⁸ Section 6 of the Offensive Weapons Act 1996 (sale to under-16-year-olds).

¹⁹ Section 80 of the Alcoholic Liquor Duties Act 1979.

²⁰ Poisons Rules 1982 (SI 1982 No. 218).

²¹ Section 1 of the Restriction of Offensive Weapons Act 1959 (sale to anyone).

²² Section 5 of the Firearms Act 1968; for lesser guns, see the controls within section 3 of the Firearms Act 1968 (amended by section 31 of the Violent Crime Reduction Act 2006).

3. THE PROCESS OF OFFER AND ACCEPTANCE IN GENERAL²³

- 3.05 A contract is normally formed by the exchange of an offer and acceptance and, usually, only between two parties. The House of Lords in *Gibson v. Manchester City Council* (1979) reaffirmed the need to apply the analysis of offer and acceptance in negotiations by sequential correspondence, notably regarding the sale of land.²⁴ The House of Lords rejected the majority decision in the Court of Appeal (Lane LJ dissenting),²⁵ where Lord Denning MR had said that offer and acceptance analysis was too rigid and out-of-date.

On the facts of the *Gibson* case (1979), the council decided to resale from proposals to sell a council house to the appellant, because the incoming Labour administration had decided to stop selling off its 'housing stock'. This was despite the fact that the price for the proposed sale had been fixed and the council had earlier assumed that the sale would proceed. The House of Lords held that the parties had yet to achieve a final agreement on the proposed purchase by a tenant of the freehold of a council house.²⁶ Reaffirming the 'conventional analysis' of offer and acceptance in such a context, Lord Diplock said:²⁷

[T]here may be certain types of contract, though I think they are exceptional, which do not fit easily into the normal analysis of a contract as being constituted by offer and acceptance; but a contract alleged to have been made by an exchange of correspondence between the parties in which the successive communications other than the first are in reply to one another, is not one of these.

- 3.06 Lord Wilberforce in the Privy Council case of *New Zealand Shipping Co. Ltd v AM Satterthwaite & Co. Ltd ('The Eurymedon')* (1975) acknowledged that not all contractual situations are easily analysed in terms of offer and acceptance, for example, jumping on an (old-style) London double-decker bus.²⁸

Similarly, Steyn LJ said in *Trentham (Percy) Ltd v. Archital Luxfer* (1993):²⁹

[I]t is true that the coincidence of offer and acceptance will in the vast majority of cases represent the mechanism of contract formation. It is so in the case of a contract alleged to have been made by an exchange of correspondence. But it is not necessarily so in the case of a contract alleged to have come into existence as a result of performance.

Furthermore, Andrew Smith J said in the *Maple Leaf* case (2009):

Although the formation of contract is conventionally analysed in terms of whether a contractual offer was accepted, the law does not require rigorous compliance with an

23 M. Furmston and G. J. Tolhurst, *Contract Formation: Law and Practice* (Oxford, 2010), chapters 2 to 4.

24 [1979] 1 WLR 294, HL.

25 [1978] 1 WLR 520, CA (Geoffrey Lane LJ dissenting).

26 *Storer v. Manchester City Council* [1974] 1 WLR 1403, CA, the sister case, which went the other way.

27 [1979] 1 WLR 294, 296–7, HL; *Wilkie v. London Passenger Transport Board* [1947] 1 All ER 258, 259, CA, per Lord Greene MR: a contract between the bus owner and passenger would not arise until a passenger had stood fully on its platform (*dictum*).

28 [1975] AC 154, 167, PC; *Clarke v. Dunraven ('The Satanita')* [1897] AC 59, HL.

29 [1993] 1 Lloyd's Rep 25, 27, CA.

analysis along these lines. Nor does it require that any particular communication or act must in itself manifest that the party intends to contract: the court will, if appropriate, assess a person's conduct over a period and decide whether its cumulative effect is that he has evinced an intention to make the contract.³⁰

In other words, there will not always be a readily identifiable exchange of articulated offer and acceptance. Instead, occasionally the courts must find consensus more flexibly.³¹ Lord Clarke in the Supreme Court in the *RTS* case (2010)³² (on which see 4.21) summarised Steyn LJ's observations in the *Trentham* case (1993) as follows:

(1) English law generally adopts an objective theory of contract formation, ignoring the subjective expectations and the unexpressed mental reservations of the parties. Instead the governing criterion is the reasonable expectations of honest sensible businessmen.

(2) Contracts may come into existence, not as a result of offer and acceptance, but during and as a result of performance.

(3) The fact that the transaction is executed rather than executory can be very relevant. The fact that the transaction was performed on both sides will often make it unrealistic to argue that there was no intention to enter into legal relations and difficult to submit that the contract is void for vagueness or uncertainty. Specifically, the fact that the transaction is executed makes it easier to imply a term resolving any uncertainty, or, alternatively, it may make it possible to treat a matter not finalised in negotiations as inessential. This may be so in both fully executed and partly executed transactions.

(4) If a contract only comes into existence during and as a result of performance it will frequently be possible to hold that the contract impliedly and retrospectively covers pre-contractual performance.

The Supreme Court in the *RTS* case (2010)³³ (on which see 4.21) also accepted the submission that conduct might override the formula 'subject to contract' (on that formula, see 12.04). But this will be unusual. In that case, Lord Clarke said:

[I]n a case where a contract is being negotiated 'subject to contract' and work begins before the formal contract is executed, it cannot be said that there will always or even usually be a contract on the terms that were agreed 'subject to contract'. That would be too simplistic and dogmatic an approach. The court should not impose

30 *Maple Leaf Macro Volatility Master Fund v. Rouvroy* [2009] EWHC 257 (Comm); [2009] 1 Lloyd's Rep 475, at [242] (affirmed on appeal, but without discussion of this point, [2009] EWCA Civ 1334).

31 Also problematic is the context of multilateral contracts: *The Satanita* [1897] AC 59, 63, HL; J. Cartwright, *Contract Law: An Introduction to the English Contract Law for the Civil Lawyer* (Oxford, 2007), 95, on *Re Recher* [1972] Ch 526, *per* Brightman J (unincorporated association; multi-party contractual matrix).

32 [2010] UKSC 14; [2010] 1 WLR 753, at [47], *per* Lord Clarke.

33 *Ibid.*, at [50], *per* Lord Clarke.

binding contracts on the parties which they have not reached. All will depend upon the circumstances.

3.07 Cross-offers. *Tinn v. Hoffman & Co.* (1873) decides that cross-offers indicate a bare coincidence of minds, but not a binding contract. This is because a simultaneous expression of interest from both sides will not disclose a sequential offer *and acceptance*, that is, there will have been no exchange of proposal and acceptance.³⁴ In this case, Grove J observed that, if X were to send Y an offer by letter, and coincidentally Y then sent an identical offer to X, but X made a speedier communication cancelling his offer, it would become troublesome if the posting of the identical offers were regarded as having already created a contract.

3.08 Acceptance: need for awareness of offer: The following propositions express general doctrine, although they were recognised in the context of unilateral contracts.

First, the offeree must be aware of the offer. This proposition is supported by *Gibbons v. Proctor* (1891).³⁵ This point can have a bearing on a person's capacity to comply with the criminal law's requirement that a car should be validly insured when driven on the public highway. In *Taylor v. Allon* (1966), a person drove his car on the public highway between expiry of the old insurance cover and commencement of the proposed new cover. He had been offered temporary insurance cover, without having explicitly accepted this offer. The Divisional Court held that the driver was covered only if he 'knew of the temporary cover and he had taken out his car in reliance on it'.³⁶

Secondly, the offeree must not have forgotten about the offer, as *R v. Clarke* (1927) (High Court of Australia) decided.³⁷

However, thirdly, the English decision in *Williams v. Carwardine* (1833)³⁸ decides that a contract can arise if the offeree responds positively to the offer (known to the offeree, and not forgotten), even though the offeree's motivation is predominantly directed at some other reason for action. In this case, a dying woman gave information entitling her to a reward – of which she was aware. She did so primarily to increase her chances 'of going to Heaven'. But the court held that this did not matter. She had satisfied the offer by providing the information. And so her estate was entitled to the promised sum.

3.09 Notification of acceptance. Normally, the acceptance must come to the offeror's attention. In the following passage in *Entores Ltd v. Miles Far East Corporation* (1955),³⁹ Denning LJ

34 (1873) 29 LT 271 (Court of Exchequer Chamber: note Hoynman J's dissent).

35 (1891) 64 LT 594; 55 JP 616; *Treitel* (12th edn, London, 2007), 2-047; A. H. Hudson, 'Gibbons v. Proctor Revisited' (1968) 84 LQR 503; P. Mitchell and J. Phillips, 'The Contractual Nexus: Is Reliance Essential?' (2002) 22 OJLS 115; cf the *New Zealand Shipping* case, [1975] AC 154, PC, in the context of third parties and exclusion clauses, at 7.63.

36 [1966] 1 QB 304, 309, Divisional Court, *per* Lord Parker CJ.

37 (1927) 40 CLR 227 (High Court of Australia).

38 (1833) 4 B & Ad 621; 110 ER 590; 5 C & P 566; 172 ER 1104; 1 Nev & M (KB) 418; 2 LJKB 101; P. Mitchell and J. Phillips, 'The Contractual Nexus: Is Reliance Essential?' (2002) 22 OJLS 115.

39 [1955] 2 QB 327, 332-4, CA.

distinguished, on the one hand, communications by telex, telephone (and he would now be bound to add, by e-mail) which are (virtually) *instantaneous* modes of communicating acceptance and, on the other hand, slow-acting communication via the mail system ('the post', or 'Royal Mail').⁴⁰

When a contract is made by post it is clear ... that the acceptance is complete as soon as the letter is put into the post box, and that is the place where the contract is made. But there is no clear rule about contracts made by telephone or by telex. Communications by these means [note, *not* by the Royal Mail] are virtually instantaneous and stand on a different footing ...

My conclusion is, that the rule about instantaneous communications between the parties is different from the rule about the post. The contract is only complete when the acceptance is received by the offeror: and the contract is made at the place where the acceptance is received.

Denning LJ illustrated this:

Suppose, for instance, that I make an offer to a man by telephone and, in the middle of his reply, the line goes 'dead' so that I do not hear his words of acceptance. There is no contract at that moment. The other man may not know the precise moment when the line failed. But he will know that the telephone conversation was abruptly broken off: because people usually say something to signify the end of the conversation. If he wishes to make a contract, he must therefore get through again so as to make sure that I heard.

However, there are two main exceptions to this general requirement that the offeror should receive notification of acceptance before a contract can arise. First, a contract can arise where the postal acceptance is *appropriately employed* (on the qualification of appropriate employment, see 3.24 to 3.26) and the letter is lost in the post without the acceptor's fault. Secondly, the offeree need not first tell the offeror of the offeree's wish to 'accept' the terms of a unilateral contract, for example, the offer of a reward for information, because here the offeror is normally *deemed* to have waived the requirement of notice (3.42); and it is enough that a person satisfies the relevant condition (for example, the return of a lost object).

- 3.10 *Timing of acceptance (other than by post)*. *Brinkibon v. Stahag Stahl* (1983) decides that notice of acceptance received in normal working hours by telex, e-mail, fax or by hand delivery is deemed to be received straightaway, even if it is not immediately read.⁴¹ If a written acceptance reaches the offeror outside that party's business hours, whether by telex, e-mail, fax or by hand delivery, acceptance occurs when business hours recommence on the next working day, at the location where the offeror is situated (probably

⁴⁰ *Ibid.*

⁴¹ [1983] 2 AC 34, HL.

'normal' working days and 'normal' working hours): *Schelde Delta Shipping BV v. Astarte Shipping BV ('The Pamela')* (1995) (also known as *Mondial Shipping & Chartering BV v. Astarte Shipping Ltd*).⁴²

The *Mondial* case itself concerned a ship-owner's contractual right to withdraw a vessel for non-payment by the charterer, and the issue was when the owner's notice of default, sent by telex, for non-payment had been received by the charterer. But the case illuminates the cognate issue of offer and acceptance. The owner's telex arrived Friday at 23.41 hours, that is, not during the charterer's business hours (of course, some businesses might be run on a 24-hour basis). The charterer's office did not open again until 09.00 hours on Monday. Gatehouse J held that the time of re-opening at the recipient's office was the moment of receipt of this notice. His judgment contains useful reference to judicial discussion:⁴³

What matters is not when the notice is given/sent/despached/issued by the owners but when its content reaches the mind of the charterer. If the telex is sent in ordinary business hours, the time of receipt is the same as the time of despatch because it is not open to the charterer to contend that it did not in fact then come to his attention (see *'The Brimnes'* [1975] QB 929, CA). See the well-known passage in the speech of Lord Wilberforce in the *Brinkibon* case [1983] 2 AC 34, 42, HL:

'I would accept [the *Entores* rule (1955)⁴⁴] as a general rule. Where the condition of simultaneity is met, and where it appears to be within the mutual intention of the parties that contractual exchanges should take place in this way, I think it a sound rule, but not necessarily a universal rule ... The [telexed] message may not reach or be intended to reach the designated recipient immediately: messages may be sent out of office hours, or at night, with the intention, or upon the assumption, that they will be read at a later time ... and many other variations may occur. No universal rule can cover all such cases: they must be resolved by reference to the intentions of the parties, by sound business practice and in some cases by a judgment where the risks should lie'

Transposed to the new electronic systems, it is submitted that this analysis provides a workable rule: that notification of an e-mailed acceptance occurs at the moment of receipt if that falls within the recipient's normal office hours; otherwise when the recipient's office re-opens for normal business.⁴⁵ To make this clear, it will be prudent for the offeror to state that an e-mailed acceptance will only occur if the e-mail (1) reaches the offeror's inbox (2) during the offeror's normal working hours. Another position, presented by Donal Nolan, is that the e-mailed acceptance should take effect as soon as the e-mail becomes accessible to the offeror (on his server or capable of being downloaded), and this rule should apply on a '24/7' basis, regardless of the offeror's ordinary business hours.⁴⁶ This would create a commercial nightmare. Why should offerors be continuously subject to e-mailed acceptance, even outside normal working hours?

42 [1995] 2 Lloyd's Rep 249; [1995] CLC 1011, Gatehouse J (also excerpted in J. Poole, *Casebook on Contract* (9th edn, Oxford, 2008), 55–9 (Poole also cites Singaporean discussion of e-mails).

43 [1995] 2 Lloyd's Rep 249, 252.

44 *Entores Ltd v. Miles Far East Corporation* [1955] 2 QB 327, 332–4, CA.

45 E. Haslam, (1996) NLJ 597, 562.

46 D. Nolan, 'Offer and Acceptance in the Electronic Age', in A. Burrows and E. Peel (eds.), *Contract Formation and Parties* (Oxford, 2010) (e-mail, and offer and acceptance).

- 3.11 There are generous ‘cooling off’ periods (periods within which a consumer can cancel a deal without legal liability) in favour of consumers who enter into agreements for the supply of goods or services either ‘away from business premises’ or by ‘distance selling’: see the Consumer Protection (Distance Selling) Regulations 2000⁴⁷ and the Electronic Commerce (EC Directive) Regulations 2002.⁴⁸
- 3.12 *Acceptance and the problem of silence.*⁴⁹ The general rule is that the offeree’s silence does not constitute consent in bilateral contracts. Two policies support this general approach. First, it is necessary to protect offerees from having contracts thrust upon them by aggressive offerors, for example: ‘Unless you respond and say “no” within [a specified period], we will infer that you have consented to my terms.’ The policy of protecting against such forced dealing is enshrined in the Unsolicited Goods and Services Act 1971 and the Consumer Protection (Distance Selling) Regulations 2000.⁵⁰ The second problem is that silence is equivocal: mistaken inferences can be drawn from a person’s failure to respond, as the House of Lords acknowledged in *Vitol SA v. Norelf Ltd* (*‘The Santa Clara’*) (1996),⁵¹ although Lord Steyn suggested that, in some situations, silence might not be equivocal and that the context might indicate clear acceptance.⁵²

[As for the suggestion] that a failure to perform a contractual obligation is necessarily and always equivocal I respectfully disagree. *Sometimes in the practical world of businessmen an omission to act may be as pregnant with meaning as a positive declaration.* While the analogy of offer and acceptance is imperfect it is not without significance that while the general principle is that there can be no acceptance of an offer by silence, our law does in exceptional cases recognise acceptance of an offer by silence. Thus in *Rust v. Abbey Life Assurance Co. Ltd* [1979] 2 Lloyd’s Rep 334 [on which see 3.17 at (3) below] the Court of Appeal held that a failure by a proposed insured to reject a proffered insurance policy for seven months justified on its own an inference of acceptance ... Similarly, in the different field of repudiation [on which see 17.46 and 17.47], *a failure to perform may sometimes be given a colour by special circumstances and may only be explicable to a reasonable person in the position of the repudiating party as an election to accept the repudiation* [as, for example, in the case of the wrongly dismissed employee who is told to pack his things and leave, and he responds in complete silence by taking all his personal items away and does not return the next day].

An illustration of the problem of equivocality is *Allied Marine Transport Ltd v. Vale do Rio Doce Navegacao SA* (*‘The Leonidas D’*) (1985),⁵³ where the Court of Appeal concluded

47 SI 2000 No. 2334 (amended by SI 2004 No. 2095, SI 2005 No. 55, SI 2005 No. 869 and SI 2008 No. 1277): *Chitty on Contracts* (30th edn, London, 2008), 2-064.

48 SI 2002 No. 2013; *Chitty on Contracts* (30th edn, London, 2008), 2-064.

49 M. Furmston and G. J. Tolhurst, *Contract Formation: Law and Practice* (Oxford, 2010), 4.62 ff.

50 *Ibid.*

51 [1996] AC 800, 811–12, HL, in the context of acceptance of repudiation: 17.46 to 17.47.

52 *Ibid.*, at 812.

53 [1985] 1 WLR 925, CA.

that many years of inactivity by a party to an arbitration reference did not unequivocally indicate implied assent to the other party's (also implied) offer to abandon the arbitration. Robert Goff LJ said:⁵⁴ 'At most, there was simply an apparent coincidence of contentment that the *status quo* should continue indefinitely, but that is not, we think, the same thing as a binding agreement that it should do so.'

- 3.13 As mentioned, the general proposition is that silence does not constitute consent. *Felthouse v. Bindley* is the decision normally cited in support of this.⁵⁵ However, the case is problematic on its facts.

In *Felthouse v. Bindley* (1861 and 1862), there had been negotiations on the price between a nephew, the prospective seller, and his uncle, a prospective buyer, for the sale of a horse. The uncle wrote, offering a compromise price. He added that, unless he heard to the contrary, he would assume that the nephew was prepared to sell at this figure. The nephew read the letter and decided he did want to sell at this price to the uncle. The nephew told the defendant, an auctioneer, not to sell the horse to any third party. But the defendant became confused and sold the horse to a third party.

The uncle sued the auctioneer in the tort of conversion, alleging that the horse had already become the uncle's property or at least that he had a right to possess the horse. The Court of Common Pleas (upheld by the Court of Exchequer Chamber) rejected this claim on the basis that no contract had arisen between the nephew and the uncle. The court further considered that it would follow that no proprietary or possessory rights could have arisen in the uncle's favour.

The suggestion that the nephew had remained inscrutably silent is puzzling on these facts because it was evident that he had manifested an intention to sell the horse to the uncle. Perhaps that decision was not quite clear-cut enough to be treated as unequivocal assent to the uncle's proposal. Another, and arguably safer, analysis would have been that the buyer has no immediate right to possession because, until the seller receives payment, the seller retains a lien over the horse. That approach would have justified the same result (for the decision enabled the courts to avoid the injustice of rendering the auctioneer strictly liable on these facts – the tort of conversion not requiring fault or bad faith).

- 3.14 As mentioned above, the rule that silence does not constitute consent is primarily designed to protect offerees. It follows that the rule should not be invoked *by an offeror* if this will cause *injustice to an offeree*. This problem can arise if the offeree has reasonably relied on an offer stating: 'Unless I hear from you to the contrary, I will assume that you accept this proposal.' In this situation, the courts ought in principle to be less reluctant to find a contract.

⁵⁴ *Ibid.*

⁵⁵ (1862) 11 CB (NS) 869; 31 LJCP 204; 10 WR 423, Court of Common Pleas; affirmed, (1863) 1 New Rep 401; 11 WR 429; 7 LT 835, Court of Exchequer Chamber; Miller, (1972) 35 MLR 489; cf *Re Selectmove* [1995] 1 WLR 474, 478–9, CA.

- 3.15 Another possible qualification upon the 'general silence rule' is that the offeree might have undertaken to break his silence *if he wishes not to be* bound. This situation was considered in a *dictum* in *Re Selectmove* (1995).⁵⁶

Peter Gibson LJ suggested that, where an offer is made by X to Y, and Y tells X that, unless he hears from Y to the contrary by a specified time, X should assume that Y has accepted the offer, Y's undertaking to get in contact with X will be binding on Y if X elects to hold Y to the bargain. This seems sound because Y is not unfairly pressurised by X. Nor is Y's failure to contact X an equivocal example of inactivity. Instead, 'it speaks volumes' because Y had made clear that silence means assent.

- 3.16 *Conduct by offeree.* The general rule that silence does not constitute consent can be displaced if a person's conduct clearly indicates that he has made an overt and free decision to accede to the proposed terms (see also 3.12).

For example, in *Nissan UK Ltd v. Nissan Motor Manufacturing (UK) Ltd* (1994), Nissan UK was the distributor of cars manufactured by Nissan Manufacturing. The parties exchanged many faxes concerning dates for the supply of cars by Nissan Manufacturing to Nissan UK, but had yet to achieve a crystal-clear agreement.⁵⁷ Then Nissan UK made a specific proposal for such a schedule of deliveries by Nissan Manufacturing. In response, Nissan Manufacturing started to deliver the cars at intervals coinciding with this schedule. The Court of Appeal held that Nissan Manufacturing's conduct did indeed speak as loudly as words: the contract had been activated by Nissan Manufacturing's implied acceptance of Nissan UK's proposal concerning the timing of deliveries. Nourse LJ encapsulated this as follows: '[I]f one of two contracting parties are toing and froing with offer and counter-offer and one maintains his proposals to the last, receiving no [verbal] comeback, it is natural to infer that subsequent conduct on the part of the other is referable to there being a contract between them and this denotes acceptance of that proposal!'

- 3.17 There are other qualifications upon the general proposition that silence does not constitute acceptance:

- (1) *Unilateral contract.* An offer of a unilateral contract (3.42) is generally taken to dispense with the need for the offeree to communicate acceptance: the offeree is not prejudiced since only the offeror in this situation will assume an obligation.
- (2) *Course of dealing between the parties: repeat transactions.* Acceptance by silence can occur if there have been repeated dealings.⁵⁸
- (3) *Silence by party initiating solid proposal for a deal.* As discussed below, if X starts the negotiations, and receives an offer or counter-offer from Y, on which X 'sits' for

⁵⁶ [1995] 1 WLR 474, 478F, CA.

⁵⁷ Court of Appeal December 1994, unreported (the case was contested by two leading counsel, Gordon Pollock QC and Lord Grabiner QC).

⁵⁸ *Treitel* (12th edn, London, 2007), 2-043.

a significant period, X's silence might be treated as consent; for, in this context, X cannot complain that he has been taken by surprise.⁵⁹

In Rust v. Abbey Life Assurance Co. Ltd (1979),⁶⁰ the defendant had acted on the claimant's request to open an investment bond and the claimant had earlier sent a cheque for this bond. But the claimant now sought the return of her money. The first ground of decision was that the claimant had made an offer to the defendant which the latter had accepted by conduct. But a second ground of decision emerged. Even if the offer in fact emanated from the defendant, who had sent the relevant policy to the claimant, the claimant's substantial delay in acquiescing in receipt of that policy, and not seeking to cancel the apparent deal, was enough to indicate assent.⁶¹

4. POSTAL ACCEPTANCES

3.18 The so-called 'postal rule' has lasted for nearly two centuries.⁶² The rule states that the offeree's acceptance occurs at the moment of posting, using the Royal Mail (but does not apply to hand delivery, faxes or e-mail, etc., 3.19). The rule favours the offeree who is immediately protected against the risk that the offeror had earlier attempted to revoke the offer. The offeree is protected against that risk, provided:

- (1) posting was also neither expressly nor impliedly ruled out (3.26);
- (2) posting was appropriate (for example, the post was not known to be affected during the relevant period by industrial disputes, 3.24, 3.25);
- (3) the offeree had not been at fault (for example, by failing to address the letter correctly, 3.22); and
- (4) the offeree had not become aware that the offer had been revoked (3.35, 3.36) (nor had reasonable access to information which would indicate this, 3.21).

As we shall see, this controversial and complex Victorian rule has proved troublesome in some contexts.

3.19 The postal rule applies to inland postal acceptance using the Royal Mail, but does *not* apply to acceptances by faxes (see below) or e-mail (see the quotation below) (nor by telex, now obsolete). The Court of Appeal in *Entores v. Miles Far East Corporation* (1955) regarded these non-postal forms of acceptance as 'virtually instantaneous'.⁶³

⁵⁹ *Ibid.*, at 2-046, on *obiter* aspect of *Rust v. Abbey Life Assurance Co. Ltd* [1979] 2 Lloyd's Rep 334 (for comment, see Lord Steyn in *Vitol SA v. Norelf Ltd* ('*The Santa Clara*') [1996] AC 800, 812, HL).

⁶⁰ [1979] 2 Lloyd's Rep 334, CA.

⁶¹ *Ibid.*, at 340.

⁶² S. Gardner, 'Trashing with Trollope: A Deconstruction of the Postal Rules in Contract' (1992) 12 OJLS 170.

⁶³ [1955] 2 QB 327, 332, CA, *per* Denning LJ.

As for faxes,⁶⁴ Colman J said in *JSC Zestafoni G Nikoladze Ferroalloy Plant v. Ronly Holdings Ltd* (2004):⁶⁵

A fax is a form of instantaneous communication: if a message has not been received, the sender is informed by his machine. Most machines also indicate to the sender whether the message has been effectively as distinct from only partly received. Accordingly, by analogy with telegrams and telex messages (see *Entores Ltd v. Miles Far East Corporation* (1955),⁶⁶ as approved by the House of Lords in *Brinkibon Ltd v. Stahag Stahl und Stahlwarenhandelsgesellschaft mbh* (1982)),⁶⁷ the agreement to appoint [X] as sole arbitrator was made when on 30 May the fax was received in England. That was the place where the contract was made.

E-mail is also classified as 'virtually instantaneous', as *Bernuth Lines Ltd v. High Seas Shipping Ltd ('The Eastern Navigator')* (2005) shows (the case concerned the effectiveness of e-mailed notice of an arbitration reference):⁶⁸

[A]rbitrations are usually conducted by businessmen represented by, or with ready access to, lawyers ... There is no reason why, in this context, delivery of a document by e-mail – a method habitually used by businessmen, lawyers and civil servants – should be regarded as essentially different from communication by post, fax or telex.

That is not to say that clicking on the 'send' icon automatically amounts to good service. The e-mail must, of course, be despatched to what is, in fact, the e-mail address of the intended recipient. It must not be rejected by the system. If the sender does not require confirmation of receipt he may not be able to show that receipt has occurred. There may be circumstances where, for instance, there are several e-mail addresses for a number of different divisions of the same company, possibly in different countries, where despatch to a particular e-mail address is not effective service.

But in the present case none of those difficulties arise. The e-mail of 5th May 2005 and, so it would appear, all subsequent e-mails, were received at an e-mail address that was held out to the world as the, and so far as the evidence shows, the only e-mail address of Bernuth. Someone looked at the e-mails on receipt and, apparently, decided that they could be ignored, without making any contact with the sender. The position is, to my mind, no different to the receipt at a company's office of a letter or telex which, for whatever reason, someone at the company decides to discard. In both cases service has effectively been made, and the document received will, in the first instance, be dealt with by a clerical officer.

64 *Treitel* (12th edn, London, 2007), 2-032.

65 [2004] EWHC 245 (Comm); [2004] 2 Lloyd's Rep 335, at [75].

66 [1955] 2 QB 327, CA.

67 [1982] 1 Lloyd's Rep 217, HL.

68 [2005] EWHC 3020 (Comm); [2006] 1 Lloyd's Rep 537, at [28] to [31].

The main incidents of the postal rule will now be explained.

- 3.20 *Posting before discovering attempted revocation.* As soon as the acceptance is properly posted, the offeror can no longer revoke the offer. *Byrne v. Van Tienhoven* (1880) decides that the offeror's revocation of the offer must *be known to*, or at least *reached*, the offeree before the latter posts a letter of acceptance.⁶⁹ If not, posted acceptance will be effective. There would probably be no contract if the offeror's revocation reached the acceptor before the latter posted his acceptance, *but* at the time of posting the acceptor had failed to open his mail or check his inbox. This last proposition is deducible from *The Brimnes* (1975), concerning an unread telex,⁷⁰ in which the court held that the recipient of that telex had effective notice of its contents once the communication had intelligibly appeared on his machine during normal office hours.
- 3.21 *Place of formation.* The contract is formed at the place where the acceptance letter is posted. The place of formation is important in establishing a 'connecting link' between the contract and the jurisdiction of the English courts. The Civil Procedure Rules 1998 (CPR) permit the English courts to give permission for a claim form to be served outside the UK and the EU where the relevant contract was formed within the English jurisdiction.⁷¹ By contrast, in the case of a fax, the place of receipt fixes the location of the contract.⁷²
- 3.22 *Delayed postal acceptance.* The moment of posting is normally decisive even if the letter is then delayed in transmission, without this being attributable to the acceptor's fault (for example, provided the latter had not carelessly omitted the postcode or used the wrong address). Toulson J in *LJ Korbetis v. Transgrain Shipping BV* (2005) acknowledged this point in a *dictum* (the case was not concerned with posted acceptance but with a fax sent negligently to the wrong telephone number), and he approved the following passage in *Chitty on Contracts*:⁷³

A letter of acceptance may be lost or delayed because it bears a wrong or an incomplete address, or because it is not properly stamped. Normally such defects would be due to the carelessness of the offeree, and although there is no English authority precisely on point, it is submitted that the postal rule should not apply to such cases. Although an offeror may have to take the risk of accidents in the post, it would be unreasonable to impose on him the further risk of the acceptor's carelessness. These arguments do not apply where the misdirection is due to the fault of the offeror, e.g.

69 (1880) 5 CPD 344.

70 *The Brimnes* [1975] QB 929, CA (withdrawal of offer effective when telex received during ordinary business hours, even if not in fact read).

71 Practice Direction 6, para. 3.1(6)(a) in the Civil Procedure Rules 1998; perhaps indicating posting rule applicable to UK outward-bound posting.

72 *JSC Zestafoni G Nikoladze Ferroalloy Plant v. Ronly Holdings Ltd* [2004] EWHC 245 (Comm); [2004] 2 Lloyd's Rep 335, at [75].

73 [2005] EWHC 1345 (QB), at [15], citing *Chitty on Contracts* (30th edn, London, 2008), at 2-058 (as the passage is now numbered).

where his own address is incompletely or illegibly given in the offer itself. In such a case, the offeror shall not be allowed to rely on the fact that the acceptance was misdirected, except perhaps where his error in stating his own address was obvious to the offeree, for in such a case the offeror's fault would not be the effective cause of the misdirection of the acceptance. It is submitted that a misdirected acceptance should take effect, if at all, at the time which is least favourable to the party responsible for the misdirection.

- 3.23 *Lost postal acceptance.*** The high-water mark of the postal rule is the Court of Appeal's majority decision in *Household Fire Insurance Co. v. Grant* (1879),⁷⁴ which decides that posting is enough even if the letter never reaches the offeror, provided it was properly stamped and addressed and the delay was not otherwise attributable to the offeree's fault.

The defendant offered to buy 100 shares in the claimant company. The claimant sent a letter accepting this offer. The letter never arrived. Upholding the claim by the claimant company's liquidator, the Court of Appeal held that the defendant was liable to pay for the shares. Thesiger LJ, a member of the majority, said that this approach could be justified on either of two grounds. First, he suggested the theory that the Post Office was the common agent of the parties, so that posting would take immediate effect, irrespective of accidents within the postal system. Secondly, he suggested that, otherwise, it would be necessary to determine whether the acceptance had reached the offeror, and this might give rise to fraud and delay. A third suggestion (which is really no more than a restatement of the rule's effect) is that the risk of postal delay or complete postal failure is borne by the offeror. He can avoid this risk by specifying that acceptance must actually reach him (which was the result in the *Holwell* case (1974),⁷⁵ 3.26).

- 3.24 *Appropriateness of postal acceptance.*** The offeree can invoke the postal rule if the offeror stipulated that acceptance should be by post (which will be rare), or if posting was objectively 'reasonable', having regard to the nature of the proposed transaction and the practicalities of effective communication by this rather slow mode. This second route is illustrated by *Henthorn v. Fraser* (1892).⁷⁶

The offeree received a written offer from the offeror when he visited the latter's Liverpool office. The offeree went home to Birkenhead, a distance of some miles, to think over the proposal. He then posted his acceptance from Birkenhead. The court regarded postal acceptance as reasonable because the offeree's home and the offeror's offices were separated by a significant distance.

⁷⁴ *Household Fire Insurance Co. v. Grant* (1879) 4 Ex D 217, CA (note Bramwell LJ's dissent); Scots law is different: *Mason v. Benhar Coal Co.* (1882) 9 R 883.

⁷⁵ [1974] 1 WLR 155, CA.

⁷⁶ [1892] 2 Ch 27, CA.

Henthorn v. Fraser shows, as was already clear from *Tinn v. Hoffman & Co.* (1873),⁷⁷ that offer and acceptance need not be communicated by the same medium. For example, in the *Tinn* case, the court had said that, if A invites acceptance by post, giving a specified time for acceptance, B can legitimately accept by some other method, provided this is no less speedy than the post.

- 3.25 The courts will not expect instantaneously communicated responses to complicated and delicate proposals. The postal rule continues to operate in such circumstances. Of course, sometimes special and temporary difficulties, known by the offeree or the public, will render the post unsuitable: for example, normal service has been, or is about to be, disrupted by a strike or national petrol shortage. In such circumstances, it would not be prudent to use the post, at any rate when time is pressing because the deadline for acceptance is imminent, and instead acceptance by phone or e-mail might be reasonably expected. But, in other situations, where acceptance is not time-specific and there is adequate opportunity to use the post, the postal mode might be wholly appropriate: everything must depend on the circumstances.
- 3.26 The Court of Appeal in *Holwell Securities Ltd v. Hughes* (1974) examined the issue of when the postal rule might be expressly or impliedly excluded by the offeror.⁷⁸ It was held that this rule can be 'disapplied' by clear or adequate language contained in the offer. But the case perhaps goes further, because Lawton LJ added a *dictum* that the rule will also be 'disapplied' if, objectively, it would be absurd to treat the moment of posting as decisive. This might be the appropriate inference if the offeror has imposed a clear deadline for successful acceptance. *Holwell Securities Ltd v. Hughes* (1974) concerned an attempted acceptance by an option-holder for the purchase of land. The option was granted on 19 October 1971 and had to be exercised within six months thereafter. The offeree posted acceptance on 14 April 1972 (with five days to spare), but the letter never arrived. The terms of the option required 'notice [of acceptance] ... to' the offeror. The Court of Appeal held that this wording was sufficiently explicit so as to require actual notice of acceptance to reach the offeror. This was the decision of both Russell and Lawton LJ. Therefore, the date of posting was not the critical date. But Lawton LJ went further. Even in the absence of a clear requirement, expressly made, he suggested that, in this context, posted acceptance would need to reach the offeror. He referred to the manifest good sense that an option grantor should actually become aware whether the option had been accepted (and similarly, perhaps, in other contexts).⁷⁹ This was a *dictum* not necessary for the decision (the case having already been decided on the basis that 'notice ... to' explicitly connotes the need for actual receipt of acceptance). Lawton LJ's *dictum* broadens the position: his *suggestion* is that the postal rule should not apply if, in a particular case, this rule 'would produce manifest inconvenience and absurdity'. He said:⁸⁰

77 (1873) 29 LT 271 (Court of Exchequer Chamber).

78 [1974] 1 WLR 155, CA.

79 But assent to third party promise rights, section 2(2)(b) of the Contracts (Rights of Third Parties) Act 1999, requires notification of acceptance by third party, by letter or otherwise, *to reach the promisor*: 7.49.

80 [1974] 1 WLR 155, 161, CA.

First, [the rule that posting concludes the contract even if the letter is lost] does not apply when the express terms of the offer specify that the acceptance must reach the offeror.

Secondly, it probably does not operate if its application would produce manifest inconvenience and absurdity ... Is a stockbroker who is holding shares to the orders of his client liable in damages because he did not sell in a falling market in accordance with the instructions in a letter which was posted but never received? ...

[T]he factors of inconvenience and absurdity are but illustrations of a wider principle, namely, that the rule does not apply if, having regard to all the circumstances, including the nature of the subject matter under consideration, the negotiating parties cannot have intended that there should be a binding agreement until the party accepting an offer or exercising an option had in fact communicated the acceptance or exercise to the other. In my judgment, when this principle is applied to the facts of this case it becomes clear that the parties cannot have intended that the posting of a letter should constitute the exercise of the option.

Lawton LJ linked this suggestion to the search for the parties' *implicit intention* when he concluded: 'the factors of inconvenience and absurdity are but illustrations of a wider principle', namely, the objective determination that, in a particular context, 'the negotiating parties cannot have intended that there should be a binding agreement until the party accepting an offer ... had in fact communicated the acceptance'.

This important *dictum* concerning 'manifest inconvenience and absurdity' should be adopted whenever it would be nonsensical to permit acceptance to occur at the time of posting. Two examples might be suggested:

- (1) The offer is made to rival bidders, the offeror requesting each to make a sealed fixed bid. In this context, the offeror needs to discover by a specified date whose purported acceptance has 'won' (illustrated by the *Harvela* case, discussed at 3.53 ff). Without receipt of hard information, the bidding process will be stultified or delayed unsatisfactorily.
- (2) But, even when the offer is made to a designated *individual*, and the immediate problem of distinguishing rival bids does not arise, but the offeror has specified a deadline for a response, it is possible that posting prior to the deadline will not be enough and that the *dictum* concerning 'manifest inconvenience and absurdity' will govern, so as to require receipt of acceptance before the deadline. (A qualification arises where special legislation operates in favour of a party issuing a rent review notice, or other notices concerning real property, and where use of registered post or recorded delivery fixes the addressee with effective notice on a deemed date,⁸¹

81 *WX Investments Ltd v. Begg* [2002] EWHC 925 (Ch); [2002] 1 WLR 2849, Patten J, considering section 196 of the Law of Property Act 1925 (in *Holwell Securities v. Hughes* [1974] 1 WLR 155, CA, option notice not sent by registered or recorded delivery, but by *ordinary post*, and so section 196 did not apply).

sometimes even if the registered posting or (attempted) recorded delivery never arrives.)⁸²

3.27 *An unresolved issue: acceptor's second thoughts.* After dropping the letter into the post box, can the acceptor change his mind and validly send an SMS message (a 'text' message) or an e-mail to retract his acceptance, provided this arrives before the acceptance letter? Or is the acceptor bound upon posting? The point is moot in England.⁸³ (The present point is confined to the postal rule: and so the discussion summarised in the remainder of this paragraph is concerned with posted (Royal Mail) acceptances rather than e-mail or hand-delivered acceptances). There are three possible answers to this problem:

- (1) *The acceptor cannot retract the posted acceptance.* South African⁸⁴ and New Zealand decisions⁸⁵ support this position. But Colin Turpin attractively opposes this solution. He argues:⁸⁶ 'The offeror would in no way be prejudiced if the [retraction by the acceptor] were held effective ... for [the offeror] would not have known of the posting of the acceptance and could not have acted in reliance upon it.'
- (2) *Acceptor's revocation of acceptance is effective.* The second possible solution is to allow the acceptor to retract by a speedier mode. This is favoured by *Cheshire, Fifoot and Furmston*⁸⁷ (2007), Hudson,⁸⁸ Burrows,⁸⁹ a Scots decision, *Dunmore v. Alexander* (1830),⁹⁰ the Indian Contract Act 1872,⁹¹ and by English *dicta*, notably Bramwell LJ, dissenting, in *Household Fire Insurance Co. v. Grant* (1879)⁹² and by Neuberger J in *Kinch v. Bullard* (1999), whose *dictum* states that, where a person has posted a letter, he can change his mind and, using phone or other speedy mode, validly cancel the effect of the posted letter in which he purported to sever a joint tenancy. This 'speedier' cancellation will be effective provided it is received before the letter is delivered.⁹³
- (3) *Acceptor should not abuse the capacity to retract.* A third approach is that, although retraction will normally be permitted, it should be disallowed if the acceptor is behaving reprehensibly and cannily trying to 'play the market', that is, speculating at the offeror's expense by playing fast-and-loose with the postal rule in response to market

82 *WX Investments Ltd v. Begg* [2002] EWHC 925 (Ch); [2002] 1 WLR 2849, at [18], noting Neuberger J's statement in *Kinch v. Bullard* [1999] 1 WLR 423, 427.

83 A. H. Hudson, 'Retraction of Letters of Acceptance' (1966) 82 LQR 169–73.

84 South Africa: *A to Z Bazaars (Pty) Ltd v. Minister of Agriculture* (1974) (4) SA 392 (c), noted C. Turpin, [1975] CLJ 25.

85 New Zealand: *Wenckheim v. Arndt* (1874) 1 JR 73.

86 [1975] CLJ 25, 26.

87 *Cheshire, Fifoot and Furmston's Law of Contract* (15th edn, Oxford, 2007), 69–70.

88 A. H. Hudson, 'Retraction of Letters of Acceptance' (1966) 82 LQR 169.

89 A. Burrows, *A Casebook on Contract* (2nd edn, Oxford, 2009), 39.

90 Indian Contract Act 1872, sections 4 and 5.

91 Scotland: *Dunmore v. Alexander* (1830) 9 S 190.

92 (1879) 4 Ex D 216, 235–6, CA.

93 [1999] 1 WLR 423, 429, *per* Neuberger J (letter posted and *delivered*, and then destroyed by sender before addressee could read it: held that the notice was properly served under a statutory rule).

fluctuations. Treitel has proposed this third solution.⁹⁴ For example, someone (with an excess of candour) posts a letter of acceptance at 11.00 am and then telephones at 11.05 am to say 'ignore my letter of acceptance, the market has just plummeted, and it's become suddenly a very bad deal. I'm out.' Treitel's idea is based on a notion of abuse of right or perhaps good faith. But it enjoys no case law support. It seems simply moralistic to say that the acceptor should be bound when he is 'guilty' of speculating. It is also arguable that the offeror can easily protect himself from such behaviour by expressly displacing the postal rule: ('acceptance to reach me by ...').

It is submitted that solution (2) should be preferred: an overtaking retraction of an acceptance by the acceptor is effective, once the retraction comes to the other party's notice. The postal rule should not mechanically bind the acceptor to his earlier posted acceptance.

- 3.28 *Posted rejection overtaken by speedier acceptance.*⁹⁵ What if, conversely, the offeree posts a letter of rejection and then changes his mind and wishes to accept after all? Can he validly 'accept' by, for example, sending an e-mail which arrives before the rejection letter (the e-mail stating, 'I'm accepting: ignore the letter sent by Royal Mail in which I rejected the offer')? It is submitted that this is a straightforward situation. The acceptance arrived before the posted rejection. The postal rule applies only to acceptances and not to rejections. And so there has been a valid acceptance. As discussed above, it would be different if the rejection letter arrived before the acceptance communication: the offeror should then be entitled to assume that the deal is off.

5. COUNTER-OFFERS

- 3.29 A counter-offer is a clear presentation by the offeree of an alternative set of terms, or the alteration of a significant term. A counter-offer is to be distinguished from a tentative or exploratory request for further information, for example, 'can I just check you meant £1,000 and not £10,000?' Lush J made this distinction in *Stevenson, Jacques & Co. v. McLean* (1880)⁹⁶ (and the Court of Appeal in *Grant v. Bragg* (2009)⁹⁷ has acknowledged this distinction).

In the *Stevenson, Jacques* case, the defendant offered to sell iron to the claimant at 40 shillings per ton, the offer to be open for a specified time. The claimant telegraphed to ask whether delivery at that price would be spread over two months or a longer period. The defendant treated this as a rejection of its offer by way of counter-offer from the claimant. Lush J said that this was wrong: the claimant's response was a mere inquiry, and

⁹⁴ Treitel, editing *Chitty on Contracts* (30th edn, London, 2008), 2-060; and (consistently) *Treitel* (12th edn, London, 2007), 2-036; *Anson's Law of Contract* (29th edn, Oxford, 2010), 52-3, uses this argument to justify adoption of position (1) ('acceptor cannot retract'), see above.

⁹⁵ For the position concerning communicated rejections of offers see 3.39.

⁹⁶ (1880) 5 QBD 346.

⁹⁷ [2009] EWCA Civ 1228; [2010] 1 All ER (Comm) 1166, at [22], *per* Lord Neuberger MR.

the defendant's original offer remained available to be accepted by the claimant within the specified time (unless in the meantime the claimant had heard, directly or indirectly, that this offer had been withdrawn).

Lush J said of the claimant's response to the defendant's offer:⁹⁸

[T]he form of the [plaintiff's] telegram is one of inquiry. It is not 'I offer forty for delivery over two months', which would have likened the case to *Hyde v. Wrench* (1840) [on which see 3.30] ... Here [in the *Stevenson* case] there is no counter proposal. The words are, 'Please wire whether you would accept forty for delivery over two months, or, if not, the longest limit you would give.' There is nothing specific by way of offer or rejection, but a mere inquiry, which should have been answered and not treated as a rejection of the offer.

However, where the response is a clear counter-offer, the counter-offeree (that is, the original offeror) can respond in one of four ways: (1) accept the counter-offer (deal done); (2) reject the counter-offer without more; (3) reject the counter-offer but reaffirm the original offer; or (4) propose different terms, that is, make a counter-counter-offer.

- 3.30 If the response is of type (2), outright and unqualified rejection of the counter-offer, the original offer is no longer available for acceptance. The offeree has no second bite of the acceptance cherry. This was established in *Hyde v. Wrench* (1840):⁹⁹

The facts involved the following stages: (1) A offered in writing to sell to B a farm for £1,000; (2) B wrote and counter-offered £950; (3) a few weeks later, A wrote and said he could not accept this; (4) two days later, B wrote, purporting to accept A's original offer, that is, for £1,000; (5) A contested whether B had the right to revert to the original offer; (6) and so B sued for specific performance of the alleged concluded agreement to buy for £1,000. The claim failed. Lord Langdale MR held that B could not revive A's original offer. The merits of this rule are its clarity and its sound protection of the offeror. He knows that his rejection of the counter-offer leaves him unexposed to acceptance of the original offer.

The rule thus offers *protection against haggling*: otherwise the offeree could offer (on the facts of *Hyde v. Wrench*, £900, £910, £920, etc., while reserving the right to accept the original offer).

- 3.31 What of possibility (3), where the counter-offer is rejected but the original offeror reaffirms the original offer? This requires an objective and explicit indication that the offer was being replaced on the table by the original offeror. In a Canadian decision, *Livingstone v. Evans* (1925), the original offeror replied to the counter-offer 'cannot reduce price'. That was held to have kept the original offer alive.¹⁰⁰ In *Re Cowan & Boyd* (1921), another Canadian

98 (1880) 5 QBD 346, 350 (approved in a *dictum* in *Gibson v. Manchester City Council* [1979] 1 WLR 294, 302, HL).

99 (1840) 3 Beav 334; 4 Jur 1106; 49 ER 132.

100 [1925] 3 WWR 454 (Alberta Supreme Court).

decision, an offer was also held to have been ‘placed back on the table’ when the offeror said that he would call on the counter-offeror to discuss the matter further.¹⁰¹

6. BATTLE OF THE FORMS¹⁰²

3.32 This is the problem of competing proposals contained within the parties’ standard terms. The law has to decide which set of terms, if any, wins the battle to govern the contract. There are various possible solutions to this conundrum:¹⁰³

- (1) The ‘last shot’ counts, and thus victory goes to the party proposing its own terms as the final part of the sequence of terms, provided the other side acquiesces. This theory was adopted in *Butler Machine Tool Co. Ltd v. Ex-Cell-O Corporation (England) Ltd* (1979)¹⁰⁴ (the leading case on this subject; see 3.33) and earlier in *British Road Services Ltd v. Arthur V. Crutchley & Co. Ltd* (1968).¹⁰⁵ In the latter case, A had delivered whisky to B for storage on A’s terms. B stamped this standard form with its own terms, and A’s driver then handed over the goods. The Court of Appeal held that the last act by B’s driver, stamping the document, was effective to render delivery subject to B’s terms. Lord Pearson, sitting in the Court of Appeal, emphasised that there had been a course of dealing between A and B and that B’s terms were standard in the warehousing industry.¹⁰⁶ As we shall see in 3.34, this approach was also confirmed by the Court of Appeal in *Tekdata Intercommunications v. Ampenol Ltd* (2009).¹⁰⁷
- (2) The court might impose the usual implied terms (that is, the ‘default’ rules supplied by common law or under statute).
- (3) The court might create an amalgam of the parties’ competing terms (‘picking and choosing’).
- (4) Finally, the court might declare that there is no contract, leaving the parties to restitutionary remedies for the value of goods or services supplied and used or enjoyed.

English law has adopted the first approach.

For the position under the ‘soft law’ codes, see PECL, *Principles of European Contract Law*, Article 2:209, stating that ‘general conditions form part of the contract to the

101 [1921] 61 DLR 497 (Ontario Supreme Court App Div).

102 M. Furmston and G. J. Tolhurst, *Contract Formation: Law and Practice* (Oxford, 2010), 4.122 ff; J. Adams, [1983] JBL 297; S. Ball, (1983) 99 LQR 572; E. McKendrick, (1988) 8 OJLS 197; R. Rawlings, (1979) 42 MLR 715; for the approach to the ‘battle of forms’ in other jurisdictions or transnational ‘soft law’: E. McKendrick, *Contract Law: Text, Cases and Materials* (4th edn, Oxford, 2010), 92–3, considering the UN Vienna Convention on Contracts for the International Sale of Goods (Article 19(2) and (3)), the *Principles of European Contract Law* (Articles 2:208 and 2:209), the Uniform Commercial Code (USA) (Article 2.207) and UNIDROIT’s *Principles of International Commercial Contracts* (Article 2.1.11).

103 S. Vogenauer and J. Kleinheisterkamp (eds.), *Commentary on the UNIDROIT Principles of International Commercial Contracts* (Oxford, 2009), 341–7.

104 [1979] 1 WLR 401, 405H, 406D, 407E, CA.

105 [1968] 1 All ER 811, CA.

106 *Ibid.*, at 817.

107 [2009] EWCA Civ 1209; [2010] 1 Lloyd’s Rep 357.

extent that they are common in substance’;¹⁰⁸ and UNIDROIT’s *Principles of International Commercial Contracts* (2004), Article 2.1.22,¹⁰⁹ stating that ‘a contract is concluded on the basis of the agreed terms and of any standard terms which are common in substance unless one party clearly indicates in advance, or later and without undue delay informs the other party, that it does not intend to be bound by such a contract’.

To illustrate the problem of the ‘battle’ between standard forms, suppose that A, the supplier, offers goods to B on A’s standard payment terms: £1,000 per unit, payable by B without discount, payment to be made within thirty days. B’s competing set of terms are that B, as prospective buyer, will order goods at £1,000 per unit with 10 per cent discount if B pays within ninety days. A then delivers the goods with an invoice which reasserts A’s terms. B’s warehouseman signs this. This signature is effective to incorporate A’s terms. In this situation, the *possible* options (for the English approach, see the following discussion) are: (a) A’s terms apply (£1,000); or (b) B’s discount terms apply (£900); or (c) the court might ‘split the difference’ between the parties (£950); or (d) conclude that the parties have failed to reach any agreement and award A the reasonable market value of the goods at the time of delivery (say, £1,100). English law is clear: applying the ‘last shot’ approach (see (1) above), solution (a) governs this case. Thus, A’s terms have prevailed because B has accepted A’s terms. B must pay £1,000.

- 3.33 In the leading decision, *Butler Machine Tool Co. Ltd v. Ex-Cell-O Corporation (England) Ltd* (1979),¹¹⁰ the majority of the Court of Appeal, consisting of Lawton and Bridge LJ, adopted the ‘last shot’ approach (confirmed in *Tekdata Intercommunications v. Ampenol Ltd* (2009), 3.34).¹¹¹

In the *Butler* case (1970), A offered to sell machine tool equipment to B, delivery in ten months’ time. A sought to protect itself by a price-escalation clause, to allow an increase in price at the date of delivery. B’s reply contained its own standard terms, without a price-escalation clause. A returned B’s ‘tear-off’ slip but added a rider saying that A was entering the contract on A’s terms. But the court regarded this rider as merely a confirmation of the subject matter. So it was not the last shot, but a broken arrow. A sought to invoke the price-escalation clause. The court unanimously held that A was bound by B’s terms. The majority applied the ‘last shot’ approach in favour of B, regarding A’s apparent ‘last shot’ as the firing of a blank cartridge.

However, in the *Butler* case (1979), Lord Denning MR, in the minority, reached the same result on the facts, but employed a range of alternative analyses:¹¹²

108 A. D. M. Forte, in H. MacQueen and R. Zimmermann (eds.), *European Contract Law: Scots and South African Perspectives* (Edinburgh, 2006), chapter 4.

109 2nd edn, Rome, 2004; see M. J. Bonell (ed.), *The UNIDROIT Principles in Practice: Case Law and Bibliography on the UNIDROIT Principles of International Commercial Contracts* (2nd edn, Ardsley, NY, 2006), 156 ff; S. Vogenauer and J. Kleinheisterkamp (eds.), *Commentary on the UNIDROIT Principles of International Commercial Contracts* (Oxford, 2009), 341 ff.

110 [1979] 1 WLR 401, 405H, 406D, 407E, CA.

111 [2009] EWCA Civ 1209; [2010] 1 Lloyd’s Rep 357.

112 [1979] 1 WLR 401; *ibid.*, at 404H–405D, suggesting that approaches (1), (2), (4) or even the last shot approach might apply to other facts.

(1) *The last shot*. 'In some cases the battle is won by the man who fires the last shot. He is the man who puts forward the latest terms and conditions: and, if they are not objected to by the other party, he may be taken to have agreed to them.'

(2) *The first shot*. 'In some cases the battle is won by the man who gets the blow in first. If he offers to sell at a named price on the terms and conditions stated on the back, and the buyer orders the goods purporting to accept the offer – on an order form with his own different terms and conditions on the back – then if the difference is so material that it would affect the price, the buyer ought not to be allowed to take advantage of the difference unless he draws it specifically to the attention of the seller.'

(3) *Both sets construed together*. 'There are yet other cases where the battle depends on the shots fired on both sides. There is a concluded contract but the forms vary. The terms and conditions of both parties are to be construed together. If they can be reconciled so as to give a harmonious result, all well and good.'

(4) *Default resort to 'reasonable implication'*. 'If differences are irreconcilable – so that they are mutually contradictory – then the conflicting terms may have to be scrapped and replaced by a reasonable implication.'

As for (3) and (4), such flexible approaches are favoured both by US law and by the 'soft law' international documents.¹¹³ Lord Denning's minority approach has the advantage that broad equity can be inserted into the discovery of the contractual terms. In short, this approach favours the finding of a contract on a compromise or customary basis. But the clear disadvantage of Lord Denning's approach is that it ignores the responsive analysis of the offer and acceptance process. And that orthodox approach (generally endorsed by the House of Lords in *Gibson v. Manchester City Council*, 3.05) is rooted in freedom of contract (on this principle, see 1.08). A second disadvantage of Lord Denning's minority approach is that it creates uncertainty by giving the court leeway to determine the eventual set of terms. This point should not be dismissed as some form of commercial rigidity or pedantry. The 'last shot' analysis is easy to apply because advisors are required only to consider whose terms were asserted last and acquiesced in by the opponent. Admittedly, this approach might not provide 'perfect justice' because there is an element of gamesmanship in winning this contest. But it is clear that English law would not be improved by a frequent and uncertain quest (requiring resort to arbitration or judicial determination) for 'some middle ground' whenever the parties have produced non-matching versions of the proposed terms. For these reasons, the courts

113 E. McKendrick, *Contract Law: Text, Cases and Materials* (4th edn, Oxford, 2010), 92–3, noting non-English approaches to this problem; UN Vienna Convention on Contracts for the International Sale of Goods (Article 19(2) and (3)), *Principles of European Contract Law* (Article 2:208), Uniform Commercial Code (USA) (Article 2.207) and UNIDROIT's *Principles of International Commercial Contracts* (Article 2.1.11); however, the *Principles of European Contract Law*, Article 2:209, permits 'general conflicting terms' to produce a contract 'to the extent that they are common in substance'.

should remain loyal to the majority approach in the *Butler* case, and they should resist the slippery slope of the minority approach advocated by Lord Denning (which is, furthermore, clearly not English law).

- 3.34 It is gratifying, therefore, that the Court of Appeal in *Tekdata Intercommunications v. Ampenol Ltd* (2009)¹¹⁴ has endorsed the authority of the majority decision in the *Butler* case (1979) (3.33). In the *Tekdata* case, A supplied high specification materials to T, for eventual use in the construction of Rolls-Royce aero engines. A's written terms contained an exclusion clause in favour of A, but T's written terms did not. Applying the last shot approach, a strong Court of Appeal (Longmore, Dyson and Pill LJ) accepted that it was decisive that T had acquiesced tacitly in A's terms. The judgments emphasise the benefit of commercial certainty in adhering to this established analysis.

In the *Tekdata* case, the claimant buyers and defendant sellers were part of a chain of suppliers to Rolls-Royce, aero-engine manufacturers, as ultimate purchasers. The defendants produced items to be used in the wiring within engine control systems to be installed in Rolls-Royce's aero engines. The buyers and the sellers had been doing business for many years. The buyers claimed that some items were delivered late, that they were not fit for the purpose, and that they were also of unsatisfactory quality. The buyers said that the contracts of purchase were on the terms of their purchase orders. The sellers contended that the contracts were on the terms of their acknowledgments, which excluded or limited their liability for any breach of contract.

The Court of Appeal (reversing Judge Simon Brown QC, sitting in the Birmingham Mercantile Court) held that the traditional offer and acceptance analysis had to be adopted unless the documents passing between the parties, and their conduct, showed that their common intention was that some other terms were intended to prevail. But the court made clear that to displace this traditional analysis it would be necessary to show a clear course of dealing between the parties which manifested a contrary arrangement. No such course of dealing had been proved in the present case. And so, applying this offer and acceptance analysis, the result here was that the buyer had acquiesced in the seller's terms, including an exclusion clause *prima facie* protecting the seller (this would not be the end of the matter, for the exclusion clause would be subject to statutory control under the Unfair Contract Terms Act 1977 (see the end of this paragraph), but this statutory point would require further decision).

Dyson LJ said:

[23] The so-called 'last shot' doctrine has been explained in *Chitty on Contracts* (30th Edition, 2008), at para. 2-037 as meaning that where conflicting communications are exchanged, each is a counter-offer, so that if a contract results at all (e.g. from an acceptance by conduct) it must be on the terms of the final document in the series leading to the conclusion of the contract. This

114 [2009] EWCA Civ 1209; [2010] 1 Lloyd's Rep 357.

doctrine has been criticised in *Anson's Law of Contract*, 28th Edition, 2002, p 39, as depending on chance and being potentially arbitrary, as well as on the ground that, unless and until the counter-offer is accepted, there is no contract, even though both buyer and seller may firmly believe that a contract has been made ...

[25] ... [However], the rules which govern the formation of contracts have been long established and they are grounded in the concepts of offer and acceptance. So long as that continues to be the case, it seems to me that the general rule should be that the traditional offer and acceptance analysis is to be applied in battle of the forms cases. That has the great merit of providing a degree of certainty which is both desirable and necessary in order to promote effective commercial relationships ...

[30] ... The question of whose conditions were intended to apply must be determined objectively on the basis of the proper interpretation of the documents which comprise the contract viewed objectively in their context. The focus must always be on what the parties must be taken, objectively, to have intended at the time when the contract was made.

The present appeal concerned merely a preliminary point of law. The decision, that the supplier's exclusion clause had been incorporated, does not extend to the question whether the seller's written standard term might be vulnerable as unreasonable under the Unfair Contract Terms Act 1977 (15.14 to 15.17).

7. REVOCATION AND TERMINATION OF OFFERS¹¹⁵

- 3.35 *Revocation of offer directly or indirectly: firm offers.* An offeree can safely and effectively accept the offer unless he knows of the offer's revocation (or its lapse through effluxion of time). Revocation by the offeror of the offer can be either direct, by telling the offeree to forget it, or indirect. Where the revocation is *direct*, the question is whether the offeree has in fact *discovered* or had the *reasonable opportunity to discover* that the offer is no longer open to acceptance by him. We have seen (see 3.20 on '*The Brimnes*' (1975),¹¹⁶ concerning an unread telex) that an e-mailed, posted or faxed revocation, arriving within normal working hours, will be effective to preclude valid acceptance once the offeree has had a reasonable opportunity (during normal working hours, if he is in business: for this qualification, see '*The Pamela*' (1995)¹¹⁷ at 3.10) to read the revocation. As for the *indirect* situation, a third party might tell the offeree that the offeror has acted in some way which clearly shows that the offer is no longer open to acceptance by that offeree (for a clear case of indirect revocation, see *Dickinson v. Dodds* (1876), 3.36). Treitel suggests this test: 'It is sufficient if the offeree knows from any reliable source that the offeror no longer intends to contract with him.'¹¹⁸ Treitel notes that this rule imposes a burden upon the offeree of determining whether his source is 'reliable' and thus whether the offer is

115 M. Furmston and G. J. Tolhurst, *Contract Formation: Law and Practice* (Oxford, 2010), chapter 3.

116 '*The Brimnes*' [1975] QB 929, CA (withdrawal of offer effective when telex received during ordinary business hours, even if not in fact read).

117 [1995] 2 Lloyd's Rep 249; [1995] CLC 1011, Gatehouse J: also excerpted in J. Poole, *Casebook on Contract* (9th edn, Oxford, 2008), 55–9 (Poole also cites Singaporean discussion of e-mails).

118 Treitel (12th edn, London, 2007), 2-059.

alive or dead. It is submitted that, once a 'real and genuine doubt' has reached the offeree, the offer ceases to be open for acceptance.

3.36 The leading case on *indirect* revocation is *Dickinson v. Dodds* (1876).¹¹⁹ The case decides the following points:

- (1) Even if a period for acceptance has been stipulated, the offer cannot be validly accepted once the offeree discovers that the 'deal is off' (see (2)(a) and (b) below). It would be different, however, if the offeree holds a binding option, granted by deed (5.03) or supported by consideration.
- (2) However:
 - (a) The offeror can revoke the offer by communicating this revocation directly to the other party.
 - (b) The offeror can escape liability by relying on the fact that the offeree has by some chance acquired knowledge of the offeror's decision or of conduct on the part of the offeror manifestly inconsistent with the offer remaining open for acceptance by the offeree.

In Dickinson v. Dodds (1876), on Wednesday the defendant offered to sell a house to the claimant for £800. The defendant said that the offer would be left open until 9.00 am on Friday. On Thursday, the defendant sold the house to a third party, but without letting the claimant know. The claimant quickly found out about the sale to the third party from a fourth party. The claimant was undeterred and handed over a letter of acceptance to the defendant before the Friday 9.00 am deadline.

The Court of Appeal held that the claimant's attempted acceptance was invalid. The claimant already knew from the third party of the defendant's revocation (or at least of conduct which made satisfaction of the contemplated deal between the claimant and the defendant manifestly impossible, because the subject matter, a house, is unique). The fact that the latter had gratuitously stated that the offer was open for acceptance until 9.00 am on Friday was an empty promise. It was *nudum pactum* (a bare 'moral' undertaking). It would have been different if, when he made his acceptance, the claimant had been unaware of the defendant's sale to the third party.

3.37 *Reform of the firm offer rule.* It might be objected that the offeree should enjoy protection even if he has not been granted by deed, nor – in the absence of a deed (5.03) – paid for, a binding option agreement (see the preceding paragraph). Some have posed the question: should it not be enough that the offeree has assumed that the promise to keep open the offer was binding?¹²⁰ But the response to this is that the offeree has not

¹¹⁹ (1876) 2 Ch D 463, CA.

¹²⁰ M. Spence, *Protecting Reliance* (Oxford, 1999), 116 ff; J. Gordley (ed.), *The Enforceability of Promises in European Law* (Cambridge, 2001), 279 ff (case 13, options given without a charge).

bought, nor earned the right to, legal protection: the offeror's promise was gratuitous; nor, in the absence of a deed, has the offeror solemnly bound himself to making a legally binding commitment.

In 1975, the Law Commission, in a working paper, recommended that firm offers, whether in writing or oral, made 'in the course of business', should be binding. But this has not received Parliamentary support.¹²¹ By contrast, the Dubai International Financial Centre has a firm offer rule which permits an irrevocable offer to be made without consideration: there is no need for writing and no need for a specified period.¹²² This is the Dubai system's modification of English contract law, based on the perception of this 'commercial hub' of what business people expect in the global market-place.

3.38 *Lapse of time.* An offeree might be given a specified time within which to accept, as the Court of Appeal in *Grant v. Bragg* (2009)¹²³ acknowledged. If the deadline is missed, the offer will not have been validly accepted. A separate point is that even a specified period for acceptance can be revoked by the offeror, unless the offeror has given the offeree a binding option, exercisable for a specified time: see the preceding paragraph. In the absence of a specified period, an (unrevoked) offer is open for acceptance only for a reasonable time.¹²⁴

3.39 *Communicated rejection of offer.* Some writers¹²⁵ say that any *communicated* rejection kills off the original offer, even if that response is not a counter-offer. For this proposition, *Chitty*¹²⁶ cites *Tinn v. Hoffman & Co.* (1873),¹²⁷ where Brett J said, without elaboration, that B's rejection of A's offer would get rid of the original offer. This seems sound (and the proposition was characterised as 'trite law', without citation, by the Court of Appeal in *Grant v. Bragg* (2009)).¹²⁸ Otherwise, the offeree could vacillate. This would be confusing, and would provoke litigation. Offerees should be expected to make their minds up and communicate their last thoughts (but, for the situation where a rejection letter, not yet received, is overtaken by a speedier acceptance, and the contract treated as valid, see 3.28).

121 Law Commission, *Firm Offers* (Working Paper No. 60, 1975), at [55] (but suggesting that proposed reform should apply only where the offer is expressed to be irrevocably open for a definite period, not exceeding six months).

122 Article 17(2)(a) of the Contract Law, www.difc.ae/laws-regulations/ (Dubai International Financial Centre).

123 [2009] EWCA Civ 1228; [2010] 1 All ER (Comm) 1166, at [25], *per* Lord Neuberger MR (and the point was further accepted as basic common law doctrine in *Gibbon v. Manchester City Council* [2010] EWCA Civ 726; [2010] 1 WLR 2081, at [16], *per* Moore-Bick LJ).

124 Toulson J in *LJ Korbetis v. Transgrain Shipping BV* [2005] EWHC 1345 (QB), at [18]; *Treitel* (12th edn, London, 2007), 2-064, 2-065, citing *Ramsgate Victoria Hotel Co. Ltd v. Montefiore* (1866) LR 1 Ex 109.

125 J. Cartwright, *Contract Law: An Introduction to the English Contract Law for the Civil Lawyer* (Oxford, 2007), 103; *Chitty on Contracts* (30th edn, London, 2008), 2-090.

126 *Chitty on Contracts* (30th edn, London, 2008), 2-090.

127 (1873) 29 LT 271, 278 (Court of Exchequer Chamber).

128 [2009] EWCA Civ 1228; [2010] 1 All ER (Comm) 1166, at [17], *per* Lord Neuberger MR (and, although less clearly, at [22]).

8. ACCEPTANCE IN THE CONTEXT OF UNILATERAL CONTRACTS

3.40 A unilateral contract is typified by the offer of a reward: ‘If you find my lost cat, I will pay you £1,000.’ Occasionally, the issue is: when is a unilateral contract accepted?¹²⁹ Three propositions can be made:

- (1) A unilateral contract is normally accepted by complete performance, for example, by the offeree supplying information under an offer of reward.
- (2) There is no need for the offeree(s) to say in advance: ‘Yes, we accept your proposal and will do our best to find your cat.’ This is because the offeror is deemed to have waived the need for such formal acceptance.
- (3) It appears that, in general,¹³⁰ the offeror cannot lawfully revoke once the offeree starts to perform. It is debatable though how point (3) is best explained: some favour the view that this is because *performance constitutes acceptance*; others consider that the performing party’s legal protection rests on an *implied collateral contract* arising prior to final acceptance by performance. It is also unclear whether commencement of performance should *always* have the effect of fettering the offeror: the sensible view, supported by at least one case, is that ‘it must all depend on the context’.

And so, in response to the uncertainties referred to in (3) above, it will be suggested here:

- (1) The better view is that the offeror’s principal duty (normally, payment of money) arises (the contract then being ‘accepted’) only when the offeree has satisfied the stipulated condition.
- (2) However, if the offeree has started to perform, an ancillary duty will sometimes arise; this will be appropriate only if it would be unjust for the offeror to revoke the offer; and that must depend on various factors (3.45).

3.41 The three main English cases on acceptance of unilateral contracts are *Carlill v. Carbolic Smoke Ball Co.* (1892),¹³¹ *Errington v. Errington & Woods* (1952)¹³² and *Luxor (Eastbourne) Ltd v. Cooper* (1941).¹³³ These will be discussed at 3.42, 3.43 and 3.45, respectively. Before examining them, it will be convenient to note Longmore LJ’s summary of this topic in *Soulsbury v. Soulsbury* (2007).¹³⁴ In the *Soulsbury* case, an ex-husband promised to leave

129 *Carlill v. Carbolic Smoke Ball Co.* [1893] 1 QB 256, CA; *Errington v. Errington & Woods* [1952] 1 KB 290, CA; *dicta* in *Daulia v. Four Millbank Nominees* [1978] Ch 231, CA; cf *Luxor (Eastbourne) Ltd v. Cooper* [1941] AC 108, HL; other cases on unilateral contracts, *New Zealand Shipping Co. Ltd v. AM Satterthwaite & Co. Ltd* (*‘The Eurymedon’*) [1975] AC 154, PC; and *Harvela v. Royal Trust Bank of Canada* [1986] AC 207, HL.

130 Cf *Luxor (Eastbourne) Ltd v. Cooper* [1941] AC 108, HL; on which see McKendrick, *Contract Law* (8th edn, London, 2009), 3.13; P. S. Atiyah, *Essays on Contract* (Oxford, 1987), 203 ff.

131 [1893] 1 QB 256, CA.

132 [1952] 1 KB 290, CA.

133 [1941] AC 108, HL.

134 [2007] EWCA Civ 969; [2008] Fam 1.

his ex-wife £100,000 in his will if she refrained from enforcing a maintenance order against him. She complied with that condition. Shortly before his death, the ex-husband remarried, and his will was revoked by operation of law, thus denying the first wife her promised sum. On his death, it was held that the first wife had a good claim to the sum against the husband's estate. In his judgment, Longmore LJ said of the *Carlill* and *Errington* cases:

Once the promisee acts on the promise by inhaling the smoke ball, by starting the walk to York [a 'class room' example] or (as here) by not suing for the maintenance to which she was entitled, the promisor cannot revoke or withdraw his offer. But there is no obligation on the promisee to continue to inhale, to walk the whole way to York or to refrain from suing. It is just that if she inhales no more, gives up the walk to York or does sue for her maintenance, she is not entitled to claim the promised sum.

- 3.42 *Carlill v. Carbolic Smoke Ball Co.* (1893)¹³⁵ is an early example of zealous judicial protection of the 'consumer'.¹³⁶ Mrs Carlill seems to fit uncannily the description of Lord Simon of Glaisdale in *Esso Petroleum Ltd v. Commissioners of Customs & Excise* (1976): 'a suburban Hampden who was not prepared to forego what he conceived to be his rights or to allow a tradesman to go back on his word.'¹³⁷ In the *Carlill* case, the Court of Appeal said that, when a contract is construed as 'unilateral', that is, one which imposes a (contingent) obligation only on the offeror, it is no objection that the offeree has not communicated acceptance. This is because the offeror has implicitly 'waived' the need for communication. Therefore, what counts is that the offeree has acted in response to, and in the manner stipulated by, the offer.

The facts of the *Carlill* case (1893) were as follows. In an advertisement in the *Pall Mall Gazette*, the Carbolic Smoke Ball Company declared that they would pay £100 to anyone who contracted influenza despite using their 'smoke ball'. They also stipulated that this device had to be used both for the period and in the manner specified. To induce custom, the company also said that £1,000 had been deposited in a bank, ready to be paid out. 'Use' of this product involved sniffing the powder several times daily for two weeks. Mrs Carlill bought the smoke ball and used it as stipulated. But she then contracted influenza. She sued for the £100 promised by the company.

The Court of Appeal upheld her claim. It held that an offer can be made to an indefinite class of people. Bowen LJ explained:¹³⁸

¹³⁵ [1893] 1 QB 256, CA.

¹³⁶ A. W. B. Simpson, 'Innovation in Nineteenth Century Contract Law' (1975) 91 LQR 247, at 263–5; and A. W. B. Simpson, 'Quackery and Contract Law: The Case of the Carbolic Smoke Ball' (1985) 14 JLS 345 (the latter is reprinted in A. W. B. Simpson, *Leading Cases in the Common Law* (Oxford, 1995), chapter 10); the *Carbolic Smoke Ball* case was applied in *Bowerman v. ABTA Ltd* [1996] CLC 451, noted by G. McMeel, (1997) 113 LQR 47–9.

¹³⁷ [1976] 1 WLR 1, 6, HL.

¹³⁸ [1893] 1 QB 256, 268, CA.

[W]hy should not an offer be made to all the world which is to ripen into a contract with anybody who comes forward and performs the condition? It is an offer to become liable to any one who, before it is retracted, performs the condition, and, although the offer is made to the world, the contract is made with that limited portion of the public who come forward and perform the condition on the faith of the advertisement. It is not like cases in which you offer to negotiate, or you issue advertisements that you have got a stock of books to sell, or houses to let, in which case there is no offer to be bound by any contract. Such advertisements are offers to negotiate – offers to receive offers – offers to chaffer, as, I think, some learned judge in one of the cases has said.

The court also held that the company had implicitly waived the need for 'acceptance' before petitioning it for the promised £100. Bowen LJ explained:¹³⁹

[A]s notification of acceptance is required for the benefit of the person who makes the offer, the person who makes the offer may dispense with notice to himself ... [A]nd if the person making the offer, expressly or impliedly intimates in his offer that it will be sufficient to act on the proposal without communicating acceptance of it to himself, performance of the condition is a sufficient acceptance without notification.

The court also held that there was 'consideration' supporting the company's promise, notably the detriment suffered in using this appliance;¹⁴⁰ or consideration might be found because the company would receive a benefit, each individual purchase tending to boost trade in the product¹⁴¹ (on the consideration doctrine, see chapter 5).

- 3.43 However, this leaves unanswered the question: when does the offeror lose the right to revoke the offer? The leading decision on that conundrum is *Errington v. Errington & Woods* (1952).¹⁴² That case generously suggests that the offeree is protected *whenever* he starts to perform, as stipulated in the offer. But this suggestion is open to doubt, as we shall see (3.46). The facts of the *Errington* case were strong and in favour of the offerees.

A father told his son and daughter-in-law: 'If you pay off the remaining mortgage instalments on this house, the property will be yours!' By saying this, the father furthermore impliedly promised that they would enjoy undisturbed possession of the property so long as they kept paying the mortgage. Acquisition of the full title, therefore, would require the couple to make all remaining mortgage payments. The couple were thus offerees.

The Court of Appeal held that they were, in the meantime, licensees. Their periodical payments were made in the hope of gaining full ownership one day. But the couple fell out, and the son went to live with his mother. Then the father, the promisor, died. The house was still occupied by the daughter-in-law (one of the original offerees). The promisor's estate tried to evict her.

139 *Ibid.*, at 269–70.

140 *The Spectator* calculated that Mrs Carlill must have sneezed over 1,000 times administering the ball to herself: Simpson, *Leading Cases in the Common Law* (Oxford, 1995), 274.

141 Similarly, *Edmonds v. Lawson* [2000] QB 501, CA (barristers' chambers gaining benefit from having pupil barristers competing for places in chambers as tenants).

142 [1952] 1 KB 290, CA; *Soulsbury v. Soulsbury* [2007] EWCA Civ 969; [2008] Fam 1, at [49] and [50].

The Court of Appeal held that the promisor's estate could not do so, so long as the daughter-in-law continued to pay off the instalments. She had not promised to pay these instalments. In other words, this was a unilateral contract: 'If you pay and continue to pay, and eventually pay all the instalments, title in the property will be transferred into your name.' Denning and Somervell LJ said that, once performance begins, the offeror cannot revoke. The offeror would be released from this duty to keep open the offer only if the offerees (originally both the daughter-in-law and the son) discontinued these payments. Denning LJ explained:¹⁴³

The father's promise was a unilateral contract – a promise of the house in return for their act of paying the instalments. It could not be revoked by him once the couple entered on performance of the act, but it would cease to bind him if they left it incomplete and unperformed, which they have not done. If that was the position during the father's lifetime, so it must be after his death. If the daughter-in-law continues to pay all the building society instalments, the couple will be entitled to have the property transferred to them as soon as the mortgage is paid off.

- 3.44 How does the *Errington* case leave the modern law? Two views are discernible: (1) that acceptance takes effect as soon as the offeree has made an unequivocal beginning to the requested performance; or (2) that commencement of performance might give rise to an implied obligation binding upon the offeror not to revoke. The second view is to be preferred.¹⁴⁴ It is supported by Reginald Goff LJ's *dictum* in *Daulia v. Four Millbank Nominees* (1978), who suggested that the courts will sometimes recognise an implied 'obligation on the part of the offeror not to prevent the condition being satisfied, which obligation ... must arise as soon as the offeree starts to perform'.¹⁴⁵
- 3.45 When will such an implied obligation be justified? The House of Lords in *Luxor (Eastbourne) Ltd v. Cooper* (1941) shows that not all offerees should receive such protection.¹⁴⁶ The House of Lords held that an estate agent was not entitled to payment of an agreed commission (or compensatory damages) even though he had 'found', and introduced to the principal/owner, a prospective buyer ready and willing to proceed. Instead, commission was not payable unless the principal/owner decided to complete a sale to the purchaser found by the estate agent. On these facts, therefore, the principal/owner was at liberty to change his mind, without triggering a liability to pay commission. The decision reflects the fact that this type of contract is 'aleatory', that is, the estate agent runs the risk of no gain if the principal/owner, for whatever reason, decides not to seal the deal. In normal times, estate agents can make a good living (although, sadly, in times of deep recession, their working lives are devoted to sharpening pencils and tidying drawers).¹⁴⁷

¹⁴³ [1952] 1 KB 290, at 295, CA.

¹⁴⁴ J. O'Sullivan and J. Hilliard, *The Law of Contract* (4th edn, Oxford, 2010), 2.73 to 2.75, attractively prefer the implied collateral contract analysis, citing Lord Cave in *Morrison Shipping Co. Ltd v. The Crown* (1924) 20 Lloyd's Rep 283, HL; C. Harpum and D. Lloyd-Jones, [1979] CLJ 31; cf *Treitel* (12th edn, London, 2007), 2-053, regards this 'ancillary obligation' analysis as 'artificial'; but why?

¹⁴⁵ [1978] Ch 231, 239, CA.

¹⁴⁶ [1941] AC 108, HL.

¹⁴⁷ P. S. Atiyah, *Essays on Contract* (Oxford, 1987), 203 ff; the problem is analogous to the question of a legitimate interest in performing under the *White & Carter v. McGregor* line of cases (18.05 ff).

Lord Russell said in the *Luxor* case (1941):¹⁴⁸

The agent takes the risk in the hope of a substantial remuneration for comparatively small exertion. In the case of the [agent] his [commission contract] was made on September 23, 1935; his client's offer [to buy the cinemas] was made on October 2, 1935. A sum of £10,000 (the equivalent of the remuneration of a year's work by a Lord Chancellor) for work done within a period of eight or nine days is no mean reward, and is one well worth a risk. There is no lack of business efficacy in such a contract, even though the principal is free to refuse to sell to the agent's client.

Other decisions establish that there is an implied term in law in an estate agency contract that, when the owner does in fact sell the relevant property to a purchaser, the selling agent must be the effective cause for securing a buyer if that agent's commission is to become payable. Otherwise, where more than one agent is used, a seller would be exposed to the risk of having to pay commission more than once.¹⁴⁹

- 3.46 Therefore, it would be inconsistent with the *Luxor* case to suppose that in all unilateral contracts the courts are prepared to protect the offeree against any form of detrimental reliance (and the wider statements of Denning LJ in the *Errington* case (1952)¹⁵⁰ and of Longmore LJ in *Soulsbury v. Soulsbury* (2007),¹⁵¹ both considered above, are simply too sweeping). Instead, such protection is appropriate only where the merits of the case require it. Relevant factors should include: (1) the nature and intensity of the offeree's reliance; (2) whether the offeror might otherwise be unjustly enriched (as on the facts of the *Errington* case); (3) whether the offeree has a strong interest in completing performance or indeed any realistic alternative (again, note the facts of the *Errington* case); and (4) whether the offeree should stoically accept his wasted efforts and disappointment, taking it 'on the chin', as one of the hazards accompanying his activity in the relevant field (as in the *Luxor* case). If, applying these criteria, it is decided that the offeree requires legal protection, the court must further decide: (1) whether the offeree should be permitted to perform and so satisfy the condition, giving him entitlement to the promised 'prize' or consideration, as on the facts of the *Errington* case (see above); or (2) whether it is enough to indemnify the offeree for the reliance loss incurred in attempting to satisfy that condition (money expended in preparation for, or partial performance of, the contemplated response).

9. AUCTIONS, TENDERS AND FIXED BID COMPETITIONS¹⁵²

- 3.47 *Auctions*. The Court of Appeal in *Barry v. Davies (trading as Heathcote Ball & Co.)* (2000)¹⁵³ awarded damages *against an auctioneer* when he refused to accept a bidder's

148 [1941] AC 108, 125–6, HL.

149 *County Homesearch Co. (Thames & Chilterns) Ltd v. Cowham* [2008] EWCA Civ 26; [2008] 1 WLR 909, at [11] ff (the case itself concerned a purchaser's agent).

150 [1952] 1 KB 290, 295, CA.

151 [2007] EWCA Civ 969; [2008] Fam 1, at [49] and [50].

152 M. Furmston and G. J. Tolhurst, *Contract Formation: Law and Practice* (Oxford, 2010), chapter 5.

153 [2000] 1 WLR 1962, CA.

acceptance of an item put up for auction without a reserve price (and perhaps the same analysis would apply when the unaccepted bid has exceeded the reserve price).

A third party's engine analysers were offered for sale by Customs & Excise at auction, and the money realised by the sale would go towards discharging the third party/owner's VAT liability. Customs had told the auctioneer to sell them without reserve. The claimant ran a car-tuning business. He saw the machines being delivered to the auction house five days before the auction. Cross, the auctioneer, said that they would be sold without reserve. The claimant attended the auction house a few minutes before noon. The law report then states:

When it came to the lots in question Cross said that the machines were to be 'sold that day' on behalf of the VAT office, that each was worth £14,000, 'ready to plug in and away you go'. He tried to obtain a bid of £5,000 to start with; there was no bid; he tried £3,000; still no response. He then asked what bids there were for the machines, and the plaintiff bid £200 for each. No other bid was made. In fact Mr Cross had received a bid from his son-in-law for £400 each; but he made no mention of this. Mr Cross then withdrew the machines from the sale.

And so the claimant's bid had not been accepted, even though it was the highest bid. The court awarded damages against the auctioneer to compensate for the bidder's 'loss of bargain', that is, the difference between the amount of the claimant's bid and the market value of the goods. It was held that the auctioneer had impliedly committed himself to a collateral contract to accept the highest bid. The consideration (the element of bargain supplied by the bidder to support this collateral contract: see chapter 5) was twofold: the bidder assumes the risk that his bid might be accepted; secondly, auctioneers receive the benefit that sales interest might be stimulated by the bidder's intervention.

The 'implied collateral' obligation is a juristic tool deployed to achieve a contractual solution in pre-contractual contexts, where the justice of the case demands. Indeed, a *leitmotiv* in the ensuing paragraphs will be the courts' willingness to construct an implied collateral obligation and, in support of this, the courts' strategic finding of 'consideration'.

- 3.48 Tenders.** A tender is an invitation to bid for a specified project, such as construction of a building, or provision of other services. There is now statutory regulation of certain types of tender, as a result of EU law. As Treitel explains:¹⁵⁴

The Common Law position ... is in some situations modified by legislation ... which gives effect to EC Council Directives, the object of which is to prevent discrimination in the award of major contracts for public works, etc., in one Member State against nationals of another Member State. These Regulations¹⁵⁵ restrict the freedom of the body seeking tenders to decide which tender it will accept and provide a remedy in damages for a person who has made a tender and is prejudiced by breach of the rules.

¹⁵⁴ Treitel (12th edn, London, 2007), 2-012.

¹⁵⁵ Public Contracts Regulations 2006 (SI 2006 No. 5) and Utilities Contracts Regulations 2006 (SI 2006 No. 6). On the first of these, see *Natural World Products Ltd v. ARC 21* [2007] NIQB 19.

3.49 At common law (for the statutory regulation of some types of tender, see 3.48) a person who invites tenders (the ‘invitor’) does not (unless he states otherwise) assume an obligation to accept any of these tenders. Thus, in *Spencer v. Harding* (1870)¹⁵⁶ (as acknowledged in *William Lacey (Hounslow) Ltd v. Davis* (1957)),¹⁵⁷ it was held that there is no duty to accept the highest tender for the purchase of goods, nor is there any duty to accept the lowest tender price for the opportunity to construct a building, etc. This *laissez-faire* approach is sound; otherwise, the invitor would have no discretion to decide which, if any, tender to accept. For example, the invitor might lack confidence in the relevant entity’s capacity to deliver on time, or might find reason to suspect that company of bad employment practices.

As for the problem of delay, consider, for example, the very late completion of the new Wembley Stadium. The building contract was won by an Australian company, which had presented a low tender. But there was a major delay in completing the stadium.¹⁵⁸ During the period of delay, the Millennium Stadium in Cardiff had to be used to host FA Cup finals and other important matches.

3.50 However, the Court of Appeal’s decision in *Blackpool and Fylde Aero Club v. Blackpool Borough Council* (1990)¹⁵⁹ imposes three obligations upon the invitor:

- (1) The invitor must ‘consider’ each valid tender. (However, at least one exception exists to this: in *Fairclough Building v. Port Talbot Borough Council* (1992),¹⁶⁰ the Court of Appeal held that the invitor had not acted wrongly when it refused to consider a particular tender because a member of the tender committee was married to a director of the relevant tendering company.)
- (2) The invitor must ignore invalid tenders.
- (3) The invitor must not ‘jump the gun’ and award the contract ahead of the deadline for submission of tenders.

These are minimal standards of fair dealing. Their recognition shows that, in this context, the English courts explicitly (for example, in the *Pratt* case (2003), discussed at 3.51) recognise a principle of good faith bargaining (generally on ‘good faith’, see 21.03 ff).¹⁶¹

The facts of the *Blackpool and Fylde Aero Club v. Blackpool Borough Council* (1990)¹⁶² case were as follows.

¹⁵⁶ (1870) LR 5 CP 561.

¹⁵⁷ [1957] 1 WLR 932, 939, Barry J.

¹⁵⁸ *Daily Telegraph*, 4 October 2007.

¹⁵⁹ [1990] 1 WLR 1195, CA.

¹⁶⁰ (1992) 62 BLR 82; 33 Con LR 24, CA.

¹⁶¹ On Commonwealth cases, see I. Duncan Wallace, (2001) 117 LQR 351–8, noting especially *Martel Building Ltd v. Canada* (2000) 193 DLR (4th) 1 (Supreme Court of Canada); and I. Duncan Wallace (1999) 115 LQR 583–6, noting *MJB Enterprises Ltd v. Defence Construction (1951) Ltd* (1999) 170 DLR (4th) 577 (Supreme Court of Canada), prescribing implied contractual obligations binding upon an invitor towards tenderers.

¹⁶² [1990] 1 WLR 1195, CA.

The defendant council invited seven organisations to tender to run a franchise at the council's airport. The deadline for submission of tenders was noon on 17 March 1983. The franchise was to fly pleasure trips over Blackpool for tourists. Three prospective franchisees responded. One of these was the claimant. It had been running the franchise under the previous contract. The claimant submitted objectively the best tender for the new franchise. But, as noted at 3.49 above, the basic rule in *Spencer v. Harding* (1870) does not give the person making the best tender the contractual right to 'win'.

In the *Blackpool* case, the claimant delivered its tender by hand (not by Royal Mail) to the council's letter box, at 11.00 am on 17 March 1983, just one hour before the deadline. But the council's janitor failed to clear the letter box until the next day. In error, the council stamped the claimant's tender bid 'late'. And so the council decided it would be improper to consider it. Instead, they awarded the franchise to a third party who had undoubtedly met the deadline for his tender. The claimant sued the council, alleging that it had been unfairly excluded from the tender competition.

The Court of Appeal held that the council had breached an implied collateral contract regulating the fair and proper management of the tendering process. On these facts, the breach was the failure to consider a valid tender made in good time.¹⁶³ The claimant was entitled to damages for loss of the chance to compete in the tender competition (although assessment of those damages was a matter remitted to the first instance court; in *Allied Maples Group v. Simmons & Simmons* (1995),¹⁶⁴ the leading modern contract case on this topic, the Court of Appeal held that there can be no recovery in respect of a lost chance if the likelihood of its occurrence cannot be regarded as 'realistic' or 'substantial': see 18.32).

In the *Blackpool* case, Bingham LJ said:¹⁶⁵

[T]he invitor does not commit himself to proceed with the project, whatever it is; he need not accept the highest tender; he need not accept any tender; he need not give reasons to justify his acceptance or rejection of any tender received. But where, as here, tenders are solicited from selected parties all of them known to the invitor, and ... [the] invitation prescribes a clear, orderly and familiar procedure ... the invitee is in my judgment protected at least to this extent: if he submits a conforming tender before the deadline he is entitled ... to be sure that his tender will after the deadline be opened and considered in conjunction with all other conforming tenders or at least that his tender will be considered if others are ... [Counsel for the claimant] was in my view right to contend for no more than a contractual duty to consider.

3.51 There is an implied duty on the part of the invitor to conduct the tender process in good faith.¹⁶⁶ This proposition, which can now be safely said to represent English law, was

¹⁶³ Stocker LJ added as a *dictum* the obligation to consider the tender in good faith: [1990] 1 WLR 1195, 1204E; on this, see the Privy Council's decision in *Pratt Contractors Ltd v. Transit New Zealand* (2003), summarised at 3.51.

¹⁶⁴ [1995] 1 WLR 1602, CA (noted by T. Church, [1996] CLJ 187); considered in *4 Eng Ltd v. Harper* [2008] EWHC 915 (Ch); [2009] Ch 91 (noted by P. Mitchell, (2009) 125 LQR 12–17).

¹⁶⁵ [1990] 1 WLR 1195, 1201–2, CA.

¹⁶⁶ [2003] UKPC 83; [2004] BLR 143; 100 Con LR 29.

approved by the Privy Council in *Pratt Contractors Ltd v. Transit New Zealand* (2003),¹⁶⁷ adopting an Australian decision, *Hughes Aircraft Systems International v. Air Services Australia* (1997)¹⁶⁸ (the same Australian decision has been adopted by a court in Northern Ireland in *Natural World Products Ltd v. ARC 21* (2007)).¹⁶⁹ In the *Hughes Aircraft* case (1997), Finn J declared that the invitor owes an obligation to adhere strictly to its *stipulated tender criteria*.¹⁷⁰ These must be applied objectively and fairly (no such *stipulated tender criteria* existed on the facts of the *Blackpool* case, 3.50).

The *Hughes Aircraft* case (1997)¹⁷¹ concerned rival tenders within the aircraft industry. The defendant ('the invitor') was a public corporation. It was responsible for the air traffic system in Australia. In response, Hughes, a Californian company, and a second company, tendered. Hughes lost. The tender invitation had requested best and final offers, and it had specified various criteria, including use of an independent auditor. Furthermore, the successful tenderer had been allowed to make a substantial reduction in its price at the last stage of the bidding.

Finn J held that the defendant had breached an implied obligation to conduct the process fairly: (1) the tender contained various criteria but these had not been applied correctly; (2) there had been a breach of confidentiality so that one bidder had been told details of the other's bid; in light of this leaked information, a revised bid had been made; and this had been illegitimately accepted.

There can be no quarrel with the *Hughes* decision in Australia. By contrast, the *Blackpool* case (3.50) in England did not concern specified and clear criteria. However, it is submitted that the courts should not cross the line beyond requiring the correct application of specified and objectively clear criteria. To go further, and so second-guess commercial judgements made in good faith and for entirely proper reasons by inviters, would unacceptably fetter the process.

The Privy Council in *Pratt Contractors Ltd v. Transit New Zealand* (2003) held that, although there is an implied duty on the part of the invitor to conduct the tender process in good faith, this does not preclude the tender committee from drawing on its members' specific knowledge of the competing parties' commercial performance and 'track record'.¹⁷² The committee was entitled to make informed commercial decisions whether to select or reject particular tenders.

In *Pratt Contractors Ltd v. Transit New Zealand* (2003), P submitted two unsuccessful tenders to T for a contract to realign a state highway. T's tender committee included Y, who knew of

¹⁶⁷ *Ibid.*

¹⁶⁸ (1997) 146 ALR 1, 35, 37, 40, 66–7, 228–9.

¹⁶⁹ [2007] NIQB 19.

¹⁷⁰ (1997) 146 ALR 1, 35, 37, 40, 66–7, 228–9 (referring to *Pratt Contractors Ltd v. Palmerston North City Council* [1995] 1 NZLR 469, 478–9).

¹⁷¹ [1990] 1 WLR 1195, CA.

¹⁷² [2003] UKPC 83; [2004] BLR 143; 100 Con LR 29.

P's business methods and engineering competence. P contended that T had breached its duty to act fairly as there was a real risk of bias due to Y's involvement in the evaluation process. The case looks to be an example of 'sour grapes' by the loser. In his judgment, Lord Hoffmann explains:¹⁷³

The duty to act fairly meant that all the tenderers had to be treated equally. One tenderer could not be given a higher mark than another if their attributes were the same. But [the tender committee] was not obliged to give tenderers the same mark if it honestly thought that their attributes were different. Nor did the duty of fairness mean that [the tender committee] were obliged to appoint people who came to the task without any views about the tenderers, whether favourable or adverse. It would have been impossible to have a [tender committee] competent to perform its function unless it consisted of people with enough experience to have already formed opinions about the merits and demerits of roading contractors.

- 3.52 *Sealed bids*. This is an arm's length competition over price, without the opportunity for revision of bids. Two or more bidders are invited to submit their best bid by a sealed bidding process. This is not an auction, because the latter (normally) requires face-to-face bidding in an auction room; whereas a bidder in a sealed bid process has only one chance to name a figure. The leading case on sealed bids is *Harvela v. Royal Trust Company of Canada* (1986).¹⁷⁴

The defendant, Royal Trust, had asked Harvela and Sir Leonard Outerbridge to submit rival sealed bids for the purchase of shares in a private company. Royal Trust said it would accept the higher bid. Sir Len's bid comprised two elements: (1) C\$2.1m (despite the Canadian currency, this was an English decision); or (2) '\$101,000 (Canadian) in excess of any other offer'. Bid (1) is a fixed bid, and bid (2) is a referential bid. In the event, Harvela's fixed bid was higher than Sir Len's fixed bid. So Royal Trust accepted Sir Len's referential bid. It awarded victory to Sir Len at a sum C\$101,000 higher than Harvela's fixed bid. The House of Lords declared that the referential bid was invalid (see further below). Harvela was the true winner. It was entitled to have the shares transferred and registered in its name, by the remedy of specific performance (18.14 ff; this equitable remedy is available to compel transfers of shares in a private company, but not in a public company).

- 3.53 The *Harvela* case (examined more fully in the next two paragraphs) establishes, therefore, two points.

- (1) A person submitting the best sealed bid is entitled (in the absence of relevant formalities: see 5.03) to receive the promised subject matter (in that case, shares in a private company); and that entitlement should be conceptualised as the bidder's successful completion of a unilateral contract: 'if you make the best sealed bid, you will be entitled to victory'.

¹⁷³ *Ibid.*, at [47].

¹⁷⁴ [1986] AC 207, HL.

- (2) The second point is that a bidder will be treated as having violated the implicit rules of the sealed bid contest if his bid is accompanied by a 'referential bid': for example, 'I furthermore bid £1,000 more than the highest fixed sealed bid' (for the possibility that capped referential bids are valid, provided the invitation makes this clear, see 3.56 (at the end of that paragraph)). The referential bid will then be invalid.

3.54 *Harvela: the unilateral contract analysis*. In his judgment in *Harvela*, Lord Diplock suggested that the sealed bidding process involved two stages. First, Royal Trust's invitation to accept the higher bid involved¹⁷⁵ a unilateral contract: if you submit, or perhaps take steps to submit, a valid higher bid, you will win, or perhaps be compensated for being denied the chance to win. The second stage is as follows: if it is clear that you are the outright winner, you are entitled to the private company shares, provided the winner pays for them; at this second stage, a contract of sale, a bilateral arrangement, has arisen. Lord Diplock explained:¹⁷⁶

The legal nature [of the invitation to bid] was that of a unilateral or 'if' contract, or rather of two unilateral contracts in identical terms to one of which the vendors and Harvela were the parties as promisor and promisee respectively, while to the other the vendors were promisor and Sir Leonard was promisee ... [U]nder neither [unilateral contract] did the promisee, Harvela and Sir Leonard respectively, assume any legal obligation to anyone to do or refrain from doing anything. The vendors, on the other hand, did assume a legal obligation to the promisee under each contract ... to enter into a synallagmatic [i.e. bilateral] contract to sell the shares to the promisee, the terms of such ... being also set out in the invitation ... The two unilateral contracts were of short duration; for the condition subsequent to which each was subject was the receipt by the vendors' solicitors on or before 3 pm on the following day ... of a sealed tender or confidential telex containing an offer by the promisee to buy the shares for a single sum of money in Canadian dollars ... If such an offer was received from each of the promisees under their respective contracts, the obligation of the promisor, the vendors, was to sell the shares to the promisee whose offer was the higher; and any obligation which the promisor had assumed to the promisee under the other unilateral contract came to an end.

3.55 The existence of Lord Diplock's suggested 'first stage' (see the preceding paragraph) would make a difference if both parties had spent thousands of pounds investigating the economic wisdom of this share purchase offer and then, *before the bids had been made*, Royal Trust had told them both that the proposed sale was being cancelled. If it were unclear who the winner would have been, it is possible that each bidder would be entitled to compensation for the amount of expenditure wasted by the invitor's cancellation of the bidding process (generally on premature termination of unilateral contracts before the offeree has performed the requested act or series of acts, see 3.43 to 3.46). Perhaps, once

¹⁷⁵ *Ibid.*, at 224.

¹⁷⁶ *Ibid.*

both parties had made their bids, it would be too late for the invitor to cancel the competition, even if he attempted to do so before the relevant deadline had expired and without having opened the relevant bids. The true winner would be entitled to be identified and claim the relevant subject matter. This would be analogous to the result in the auction case, *Barry v. Davies* (2000)¹⁷⁷ (on which see 3.47 above), where a highest bid was not 'knocked down' to the claimant, and no reserve price applied. The auctioneer was required to compensate the claimant for his loss of bargain (if he had 'knocked down' in favour of the bidder, a contract of sale would have arisen in favour of the bidder, the hammer signifying acceptance of the bidder's offer). It should be noted that the House of Lords in the *Harvela* case (3.52 ff) did not use the language of good faith. But it is clear that they were giving effect to their perception of what a fair, reasonable and objective evaluation of this context would require. Both the *Harvela* case and the *Blackpool* decisions (on the latter, see 3.50) demonstrate pliable use of the concept of an implied collateral or preliminary contractual obligations. This case-by-case or 'casuistic' style of reasoning is typically English.

- 3.56 *Harvela and the 'referential bid' issue.* In the *Harvela* case (3.52 ff), Lord Templeman gave two main reasons for rejecting Sir Leonard's attempt to make a referential bid.¹⁷⁸ First, the reason the other bidder, Harvela, had not made a referential bid was that the invitation to bid, on an objective view, did not indicate that such a 'sneaky' bid was permissible. This is the objection that the terms of the invitation expressly *or impliedly* prohibit a referential bid. Secondly, Lord Templeman noted that an impasse would emerge if more than one respondent made a referential bid (unless, where there are only two bidders, the referential bid is capped, that is, subject to a maximum figure). This is the objection based upon practicability. In the following passage, Lord Templeman contemplated the possibility that referential bids might be expressly invited, provided each was capped. He said:¹⁷⁹

It would have been possible for the vendors to conduct an auction sale through the medium of confidential referential bids but only by making express provision in the invitation for the purpose. It would not have been sufficient for the invitation expressly to authorise 'referential bids' without more ... *It would have been necessary for the invitation to require each bidder who made a referential bid to specify a maximum sum he was prepared to bid. That requirement would ensure that the sale was not abortive and that both bidders had a genuine chance of winning ...* The sale would in effect be an auction sale and produce the consequences of an auction sale because the vendors would have made express provision for bids to be adjusted and finalised by reference to the maximum bid of the unsuccessful bidder. But without such express provisions the invitation is not consistent with an auction sale.

To sum up: (1) it is possible that future cases will permit a capped referential bid to be considered, *if the invitation expressly permits a referential bid*; (2) such a permission

177 [2000] 1 WLR 1962, CA.

178 [1986] AC 207, 231–2, HL.

179 *Ibid.*, at 232–3.

should be interpreted as requiring each referential bid to be capped; and so *a person who makes an uncapped referential bid should not count*; (3) parties presenting referential bids would need to make two bids: one fixed bid, and a second referential bid subject to a cap.

10. THE OBJECTIVE PRINCIPLE OF CONSENT¹⁸⁰

3.57 The English courts recognise the so-called ‘objective principle’ of agreement. As Lord Reid said in *McCutcheon v. David MacBrayne Ltd* (1964):¹⁸¹ ‘[T]he judicial task is not to discover the actual intentions of each party; it is to decide what each was reasonably entitled to conclude from the attitude of the other.’ This principle requires a party’s language or conduct to be interpreted in the manner in which objectively and reasonably it might be understood by the other party. The principle has a large application because it will determine the following issues: whether the relevant words or conduct should be regarded as an offer, or as an invitation to treat; whether there has been an acceptance of an offer; whether a particular term is being proposed; whether a person is repudiating a contract; and whether the other party is accepting such a repudiation.

3.58 *Rationale of the objective principle.* This principle protects an addressee against the surprise and injustice which would result if the communicating party’s true but non-apparent intentions or private meanings were instead to govern.

Lord Diplock in ‘*The Hannah Blumenthal*’ (1983)¹⁸² said that the objective principle should not be understood to require actual detrimental reliance upon the language used in order to activate this principle. It is enough that the addressee can be taken to have assumed (that is, to have relied cognitively) that the objective meaning of the words would operate. (Andrew Smith J in the *Maple Leaf* case (2009) suggested – the point did not directly arise for decision in the case – that the addressee, B, cannot rely on the objective appearance that A is intending to enter into contractual relations if A’s words and conduct had neither led B to believe that A so intended, nor if B ‘had simply formed no view one way or the other as to whether [A] so intended’; for, in this situation, B has not adopted the objective inference that A was intending to contract; but it will be incumbent on A to show that B did not entertain the objective meaning.)¹⁸³

180 D. Friedmann, (2003) 119 LQR 68; J. R. Spencer, [1974] CLJ 104; W. Howarth, (1984) 100 LQR 265; J. Vorster, (1987) 103 LQR 274; M. Chen-Wishart, in J. W. Neyers, R. Bronaugh and S. G. A. Pitel (eds.), *Exploring Contract Law* (Oxford, 2009), 341 ff.

181 [1964] 1 WLR 125, HL; traced in *Shogun Finance Co. Ltd v. Hudson* [2004] 1 AC 919, at [183], to *Gloag on Contract* (2nd edn, Edinburgh, 1929), at 7 (Scots contract textbook); see also the clear statement by Lord Steyn, ‘Contract Law: Fulfilling the Reasonable Expectations of Honest Men’ (1997) 113 LQR 433–4.

182 [1983] 1 AC 834, 915–16, HL.

183 *Maple Leaf Macro Volatility Master Fund v. Rouvroy* [2009] EWHC 257 (Comm); [2009] 2 All ER (Comm) 287; [2009] 1 Lloyd’s Rep 476, at [228]; in fact, this point was *obiter* because the judge held, at [229], that the addressee did assume that the objective meaning would operate in his favour (affirmed on appeal, but without discussion of this point, at [2009] EWCA Civ 1334).

In *Shah v. Shah* (2001) (5.04), the Court of Appeal held that the covenantor's act of delivering an imperfect deed (imperfect because the deed was invalidly witnessed) to the covenantee created an estoppel by representation.¹⁸⁴ This estoppel rendered effective the technically invalid deed. The covenantee's 'reliance' on the representation was his assumption that the deed was legally valid.

The objective principle also promotes certainty and predictability. It promotes out-of-court settlement by the parties:¹⁸⁵ guided by this objective criterion, the parties are more likely to be correct in predicting the manner in which the courts will interpret disputed conduct and words. Furthermore, it facilitates decision-making. It would be hopeless for the courts to seek to discover, many months or years after the relevant facts occurred, whether a party's words or conduct had been intended by him in some sense different from their apparent meaning.¹⁸⁶

- 3.59 *Situations where there is no objective consensus.* No objective consensus can be discerned if the parties have purported to agree terms but even their explicit versions are manifestly and irreconcilably in conflict. A subtler problem emerges if, as *Raffles v. Wichelhaus* (1864) decides, parties have used the same language but on closer examination of the surrounding facts it emerges that they have referred to two distinct subject matters, producing a *latent* conflict which the courts cannot resolve¹⁸⁷ (see 4.10 for details of that case).
- 3.60 *Illustrations of the objective principle producing the conclusion that a valid contract exists.* Several situations will be examined: one party's lack of awareness of the other's insanity (3.61); one party's genuine belief that the other party is proposing an offer to the first party (3.62); and one party's genuine belief that the terms of the proposal are those stated (even if the other party has made a slip in making such a statement) (3.63).
- 3.61 *One party's insanity not known to the other.* The objective principle protects a party who is unaware of the other's mental incapacity. The Privy Council in *Hart v. O'Connor* (1985)¹⁸⁸ made clear that a contract will arise in this situation. This is a strong application of the objective principle, because (against this decision) it might be argued that there should be no contract if one party suffers mental incapacity. This was in fact the original

184 [2001] 4 All ER 138, CA, at [30] ff (witness not in room at time of covenantor's signature; non-compliance with section 1(3) of the Law of Property (Miscellaneous Provisions) Act 1989).

185 Generally on dispute resolution, whether by litigation, arbitration, mediation or settlement, see N. Andrews, *The Modern Civil Process* (Tübingen, 2008).

186 Cf St Germain, *Doctor and Student*, Book III, chapter VI, section V: 'of the intent inward of the heart man's law cannot judge'.

187 (1864) 2 H & C 906, Court of Exchequer.

188 [1985] 2 All ER 880, PC; however, where the incapax's property is subject to the control of the court, under sections 15 ff of the Mental Capacity Act 2005, transactions which would be inconsistent with the court's control of those assets will be void as against that party; *Chitty on Contracts* (30th edn, London, 2008), 8-073, and *Treitel* (12th edn, London, 2007), 12-056, 12-057.

rule. But that approach was long ago rejected by the English courts, and this application of the objective principle was confirmed in *Hart v. O'Connor* (1985).¹⁸⁹

- 3.62 *One party is unaware that the offer is not aimed at him.* If X reasonably believes that the other is making a contractual offer to him, X should be entitled to accept that proposal.

In *Moran v. University College Salford (No. 2)* (1993),¹⁹⁰ the defendant university offered Moran a place to study physiotherapy for the forthcoming academic year, which he accepted in good faith. But the offer was a clerical error. The fact that this was an error was revealed to him only in early September. University central clearing had been completed by then, and so he missed an academic year because his Salford place had been denied him at the last minute. Relying on his assumption that he had a secure place, he had quit his job and accommodation in London.

The Court of Appeal held that a contract had arisen, in accordance with the objective principle. Moran was entitled to relief. But this took the form of compensation for his detrimental reliance on the offer, rather than an order compelling the university to take him that year or in the future. It should be noted that no contract would have arisen if Moran had known – or perhaps ought reasonably to have known – of the university's mistake.

- 3.63 *One party is unaware of the other party's mistaken presentation of the terms of the proposed deal.* A contracting party cannot invoke his own mistake concerning a term if (1) the other was not aware of it; (2) nor can he be deemed to have been aware of it (on the latter permutation, see *OT Africa Lines v. Vickers plc* (1996) at 3.65); (3) nor did he induce the other's error (on this see the *Scriven Bros* case at 3.64).

In *Centrovincial Estates plc v. Merchant Investors Assurance Co. Ltd* (1983),¹⁹¹ the landlord proposed a renewal of a lease at rent of £x (but it had intended a higher rent). The tenant accepted the offer of £x. In an appeal concerning a summary judgment, the Court of Appeal held that the tenant was *prima facie* entitled to a lease at that rent, unless at trial it could be shown by the landlord that the error was apparent to the tenant. If the error were shown to be apparent, the tenant could not take advantage of it and the objective principle would then melt away.

- 3.64 *One party innocently misleads the other into mistakenly presenting or accepting terms.* X cannot take advantage of Y's error, if the latter has been led into error by misleading

189 *Molton v. Camroux* (1849) 4 Exch 17, 154 ER 1107 (Court of Exchequer Chamber), examined in *Hart v. O'Connor* [1985] 2 All ER 880, 888E; for citation of the opposite approach in Scotland, see *ibid.*, at 888A.

190 *Moran v. University College Salford (No. 2)* [1993] 4 Educ LR 187; *Independent*, 26 November 1993, CA (cf the problematic reasoning in *Upton-on-Severn Rural District Council v. Powell* [1942] 1 All ER 220: contract found for hire of fire services, even where neither party contemplated a contractual arrangement: *Treitel* (12th edn, London, 2007), 2-047).

191 [1983] Com LR 158.

conduct on X's part, even if that conduct was innocent. Conduct is enough: there is no need for a verbal misrepresentation (on misrepresentation, see chapter 9).

In *Scriven Bros v. Hindley* (1913), a buyer had successfully bid for goods at auction.¹⁹² He then tried to resile from the contract, contending that he had honestly believed he was bidding for hemp, whereas the relevant lot was 'tow', an inferior commodity. Normally, the buyer would be bound by the objective principle to pay for the tow because the other party would assume reasonably that this is what the buyer wanted. However, it appeared that the auction had been organised in a confusing manner and that this had misled the buyer. He had assumed that chalk marks on the auction floor indicated that the lot was hemp rather than tow. The judge directed the jury that the buyer could resist a claim for payment if the auctioneer, who was the seller's agent, had (even innocently) induced the buyer's understandable confusion in this way.

- 3.65 *One party's awareness of the other's mistaken presentation or acceptance of terms.* A line of cases demonstrates that errors concerning a term of the supposed transaction cannot be 'snapped up' in bad faith by the other party. In *Hartog v. Colin & Shields* (1939), Singleton J held that, if the buyer knows of the seller's error concerning the price, the buyer cannot 'snap up' the mistaken offer.¹⁹³ In *OT Africa Lines v. Vickers plc* (1996), Mance J suggested that the 'knowledge' test is wider: whether one party knew *or should reasonably have known* of the other party's error concerning price¹⁹⁴ (although, on the facts of that case, there was no reason for the offeree to have realised that the other party had become flustered over the relevant term: see further 10.17).

But the Court of Appeal in Singapore in *Chwee Kin Keong v. Digilandmall.com Pte Ltd* (2005)¹⁹⁵ held that, in the absence of A's knowledge of B's error as to terms, the Common Law is of no assistance to B, leaving only the possibility that equity might provide relief for B. To attract such equitable assistance, B would need to show that A had sufficient suspicion of B's error that it was unconscionable for A to maintain the contract. The court would then rescind the contract, to protect B. On the facts of that case, the court would then be responding to the fact that A had taken advantage, in suspicious circumstances, of a glaring error in the price at which computer equipment had been offered for sale by B.

It is submitted that in England a more straightforward approach would be adopted: (1) Was A aware of B's mistake as to terms, or at least was A sufficiently alerted to the probability that B was mistaken in this way? (2) If so, the contract is void at Common Law. (3) There is no need to revert to equity in order to render the contract voidable. This suggested unitary approach to the question gains support from a brief consideration of the Singaporean case,

¹⁹² [1913] 3 KB 564.

¹⁹³ [1939] 3 All ER 566, Singleton J.

¹⁹⁴ [1996] 1 Lloyd's Rep 700.

¹⁹⁵ [2005] 1 SLR 502, at [80] (Singapore Court of Appeal); noted by Kelvin F. K. Low, [2005] LMCLQ 423–8, and by T. M. Yeo, 'Great Peace: A DISTANT Disturbance' (2005) 121 LQR 393.

just cited, by an English Commercial Court judge, Aikens J, in the *Statoil* case (2008).¹⁹⁶ He said that the pricing error in the Singaporean case fell 'squarely within the classic rule. There was a unilateral mistake by the seller about the price of the printers. The buyers knew that the mistake had been made, but went ahead and "snapped up the offer". Plainly, when the subjective evidence was examined, the parties were not agreed as to the most fundamental term of the contract: the price.'

See the discussion at the end of 3.66 for the suggestion that, where an error as to terms is 'known to the other', the transaction, although provisionally void for unilateral error, can be ratified on the non-mistaken party's supposed terms.¹⁹⁷

3.66 *One party's awareness of the other party's mistake as to unwarranted quality, value or nature of subject matter.* Now we come to a thorny topic. This concerns 'unilateral' errors relating to the 'quality', 'attributes' or the 'utility' of the proposed subject matter, for example, of the nature of goods to be supplied following a sample of the goods at the point of sale. The starting point is the proposition that, where B knows that A is mistaken concerning the quality of the subject matter, B is under no duty to point out that error to A. It is different if (i) A's mistake concerns the supposed terms of the proposed contract, that is, A believes that there is a tacit warranty that the subject matter of the transaction, normally goods, will possess a particular characteristic or value, or that it will have a particular nature; and (ii) B knows of that type of error and stays silent; for, if (i) and (ii) are shown, the law favours A (as we shall see). It should also be noted (see further 10.17) that B will be treated as having knowledge if he ought reasonably to have known that A was mistaken in this special fashion. And so the core of the *Smith v. Hughes* doctrine is the rather subtle distinction between A's mistake as to 'quality' (old oats/new oats or pure silk/man-made fabric) and a mistake concerning the existence of an implied or express term concerning that quality (goods described as 'old oats' or 'pure silk', or goods implicitly traded as such). If A is to rebut the inference that he has objectively assented to a contract for the relevant subject matter, A needs to show (1) that he believed there was such an implied term (that the goods will have the relevant quality) and (2) that the other party, B, knew precisely that this was A's belief. In practice, this rather teasing double psychological inquiry – into A's belief and B's alleged knowledge of A's belief – will be resolved by taking an objective view. The twofold question will be whether A had a reasonable basis for believing that there was an implicit warranty that goods should be of a certain type; and whether it can be inferred safely that B must have known (or perhaps ought to have known, 10.19) that this was A's precise belief. In the absence of such a reasonable and contractual belief, A's miscalculation concerning the nature or quality of the goods is at his own risk (and B's knowledge of A's 'non-warranty belief' will make no difference, as *Smith v. Hughes* (1871) states, see text below). Instead, A will be bound to

196 *Statoil ASA v. Louis Dreyfus Energy Services LP ('The Harriette N')* [2008] EWHC 2257 (Comm); [2009] 1 All ER (Comm) 1035; [2008] 2 Lloyd's Rep 685, at [95]; J. Cartwright, 'Unilateral Mistake in the English Courts: Reasserting the Traditional Approach' (2009) *Singapore Journal of Legal Studies* 226–34.

197 R. Stevens, in A. Burrows and E. Peel (eds.), *Contract Terms* (Oxford, 2007), 101, 117.

the objective agreement, without the supposed implied term operating in his favour. The leading case is *Smith v. Hughes* (1871).¹⁹⁸

Facts

Smith v. Hughes (1871) was a common law action by a seller of oats for non-payment of the price. It was an appeal from a jury direction (in the twentieth century jury trial was abolished for claims framed in contract, and only preserved for actions in the torts of malicious prosecution, false imprisonment and defamation). The seller allowed the purchaser to sample the oats. The purchaser wanted oats to feed to his racing horses.¹⁹⁹ New oats would be likely to induce 'colic' in horses, which can prove fatal. The purchaser bought a quantity of oats without stipulating that he wanted 'old' oats (and without the seller having by words or conduct induced the buyer's error).²⁰⁰ He then refused to pay for the new oats and asserted that he was entitled to reject the goods. So the seller sued for the price.

In this case it was apparent, in accordance with the objective principle, that *prima facie* there was a valid contract for the new oats: the purchaser's own ('unilateral') mistake during the sampling process would not exonerate him from the duty to pay. However, it was necessary to consider the following twist: what if the seller knew that the other party believed the oats which he, as a prospective purchaser, had sampled were old, but the seller did nothing to disabuse him of this error? On this last point, the trial judge had wrongly directed the jury that the buyer would then have a good defence. On appeal, this direction was rejected as an error of law. Instead, the Court of Queen's Bench held that the seller's acquiescence in the buyer's error would count only if the buyer's (reasonable) belief had been that there was an implied warranty that the oats should be 'old'. If that were shown, the buyer would be entitled to reject the goods.

Buyer's uphill task

But the buyer would face an uphill task to establish an error as to terms on these facts. The sale had been concluded after the buyer had sampled the oats (he was, it seems, a farmer). Unless it was apparent to the seller that the buyer was 'out of his depth' and manifestly ignorant of the demands of a racehorse diet, the sellers could safely assume that the buyer (a racehorse owner or his staff) was competent to assess whether the sampled oats were suitable for his intended use. Furthermore, the buyer would need to show that the seller knew that the buyer believed that he had an implied warranty that the goods would be of a particular quality.

Sale of Goods Act

Smith v. Hughes was decided in 1871. Twenty-two years later, the common law sale of goods was codified by the Sale of Goods Act 1893, updated now in the 1979 Act. Section

198 *Ibid.*; on the pre-contractual duty to disclose in contracts of insurance, see 9.34.

199 The word 'oats' appears in Samuel Johnson's 1755 dictionary: 'Oats: a grain which in England is generally given to horses but in Scotland supports the people.'

200 Cf *Scriven Bros v. Hindley* [1913] 3 KB 564.

15(2) Sale of Goods Act 1979, re-enacted from the earlier legislation without change, affirms that the seller is liable only if the goods supplied did not correspond to the sampled goods, or if there is some 'defect' in the goods which the buyer could not be expected to discover from sampling. But the oats in *Smith v. Hughes* were not defective. The real problem was that they were the wrong sort. They were new, and not old.

True analysis of acquiescence in another's belief as to the existence of a term

If a buyer did believe that the seller was impliedly warranting that, for example, oats available for immediate purchase are old, and the seller knew of this error, it should follow that the contract would be composed on the buyer's assumed terms. In that situation, the buyer could reject the goods, or, if he had kept them, he could go on the offensive and sue the seller for loss caused by the failure to supply goods as implicitly warranted.

Lord Atkin in *Bell v. Lever Bros Ltd* (1932)²⁰¹ supported this analysis:

In these cases I am inclined to think that the true analysis is that there is a contract, but that the one party is not able to supply the very thing, whether goods or services, that the other party contracted to take; and therefore the contract is unenforceable by the one if executory, while if executed the other can recover back money paid on the ground of failure of the consideration [or perhaps sue for damages if the racehorse were harmed as a result of consuming the wrong type of oats].

Stevens has suggested that the result might be explained as a void contract which can be ratified, that is, activated, by the innocent party:

It is not the case that the only options are that the contract is either voidable or absolutely void for all purposes. Rather, the party making the mistake has the option to ratify a contract which would otherwise be of no effect and void ... It is void unless ratified.²⁰²

3.67 Commercial law and ethics. The aspect of *Smith v. Hughes* (1871) (see 3.66) which some find troubling, even distasteful, is the general proposition that one party can acquiesce in another's miscalculation of the subject matter's (unwarranted) nature, or 'error as to quality', or error as to value (as distinct from error as to terms, including terms containing the legally binding description of the goods). Is this not to countenance sharp practice? Blackburn J in *Smith v. Hughes* (1871) admitted²⁰³ that such behaviour is indeed morally reprehensible. But he suggested that one's sense of moral disapproval cannot be legally decisive. Legal standards should not be set too high. The courts should not be overly fastidious. The law of contract in England is administered by judges for businesses and wide-awake consumers and not by saints or philosophers intent on remedying every moral

201 [1932] AC 161, 222, HL.

202 R. Stevens, in A. Burrows and E. Peel (eds.), *Contract Terms* (Oxford, 2007), 101, 117.

203 (1871) LR 6 QB 597, 606–7.

infringement in the market-place. This robust approach is an example of the pragmatism which permeates English commercial law.

In *Thames Trains Ltd v. Adams* (2006),²⁰⁴ A, a victim of the Paddington train crash in October 1999, had sent, through his solicitor, a fax to the railway company, Thames Trains, in which he expressed willingness to accept a settlement sum paid into court (the court held that this was an offer made by A, and not an acceptance). That settlement sum was US\$9.3m. A's fax was in response to Thames Trains' statement, made an hour before, that no more money could be found. Within an hour of A's fax, but unaware of A's offer, Thames Trains raised its settlement figure by US\$500,000. A's solicitors realised that their fax had either not been received or, if received, not read. A accepted the increased settlement offer of US\$9.8m. The court held that the resulting settlement was binding. The contention that this involved a unilateral error unconscionably acquiesced in by the other side failed.

On this point Nelson J said:²⁰⁵

I do not consider that a reasonable man would expect [A's solicitor], acting honestly and responsibly, to have informed [Thames Trains' solicitor] of her earlier offer. Her conduct was not unconscionable, nor deceitful, nor sharp practice, nor was she taking unfair advantage of [Thames Trains' solicitor's] ignorance of her offer, given, in particular, that it had only been made as a result of him inaccurately informing her that no further monies were available, and that he had failed to receive it because of systems failures within his own office ... [A's solicitor] was entitled to stay silent, act in her client's best interests and accept the increased offer.

- 3.68 Lord Atkin's support for a robust approach.** In *Bell v. Lever Bros Ltd* (1932), Lord Atkin confirmed that, in general, a contracting party is not obliged to speak up and correct the other's error as to the subject matter of the proposed deal.²⁰⁶

A buys B's horse; he thinks the horse is sound and pays the price of a sound horse; he would certainly not have bought the horse if he had known as a fact that the horse was unsound. If B made no representation as to soundness and has not contracted that the horse is sound, A is bound and cannot recover the price ... A has no remedy, and the position is the same whether B knew the facts or not.

- 3.69 Lord Hoffmann's further support.** Furthermore, in the *BCCI* litigation (2002), Lord Hoffmann²⁰⁷ attractively endorsed the *Smith v. Hughes* and *Bell v. Lever Bros Ltd* doctrine: 'there is obviously room in the dealings of the market for legitimately taking advantage of the known ignorance of the other party.' This is a succinct restatement of the (commercially) obvious: that a party to negotiation is not generally required to look out for his rival negotiating party's economic interests. To require otherwise would be naïve, even commercially injurious. Much economic activity involves one party enjoying superior

²⁰⁴ [2006] EWHC 3291 (QB).

²⁰⁵ *Ibid.*, at [56].

²⁰⁶ [1932] AC 161, 224, HL.

²⁰⁷ *BCCI v. Ali* [2002] 1 AC 251, HL, at [70].

knowledge of the proposed contract's value, characteristics or application. Admittedly, doubts had been expressed in the Court of Appeal by Chadwick LJ and Scott V-C in *BCCI v. Ali*, but those sceptical remarks were tentative and unconvincing.²⁰⁸ Finally, Aikens J in the *Statoil* case (2008),²⁰⁹ noting the *Smith v. Hughes* doctrine, acknowledged that, if X is aware of Y's error, but Y's error does not concern a supposed term, the contract is valid.²¹⁰ He further held that there is no equitable doctrine of unilateral error suffered by X as to subject matter known to Y.²¹¹

3.70 *Summary of uninduced unilateral errors as to unwarranted quality, value or subject matter.* One can sum up the *Smith v. Hughes* and *Bell v. Lever Bros Ltd* doctrine as follows. First, a buyer, A (and indeed contractors generally) should look after themselves (*caveat emptor*). Secondly, the objective principle binds party A to the relevant transaction despite his economic or strategic miscalculation. Thirdly, the buyer on the facts of *Smith v. Hughes*, by way of exception to the objective principle, will have a defence to an action for the price in three situations (indeed, in situations (2) and (3) A will have a positive right of action against B for B's failure to deliver goods corresponding to the express or implied term):

- (1) B has made a positive misstatement, or by conduct B has misled A; or
- (2) A's belief concerning the subject matter of the transaction is supported by an implicit warranty, notably an implied term inserted by, for example, the Sale of Goods Act 1979, sections 12–15; or
- (3) A thought that his belief constituted an implicit warranty, and B knew this.

3.71 *'Reasonableness': a qualification upon the objective principle.* The Court of Appeal's rejection of a *contractual action* in the 'unsuccessful vasectomy case', *Thake v. Maurice* (1986),²¹² shows that the objective principle does not enable a person to rely unreasonably on the literal comments made by the opponent. 'Common-sense' non-literal interpretation will prevail, where appropriate. This proposition is a corollary of the fact that the objective principle is rooted in the notion of *reasonable interpretation* of words, oral or written, and the outward appearance of conduct.

In *Thake v. Maurice* (1986),²¹³ the claimants, husband and wife, went to the defendant, a private medical consultant, to arrange a vasectomy for the husband. The doctor told them that the operation was bound to succeed. Although the operation was an initial success, the husband later became fertile (this was both unusual and contrary to the doctor's assurance).

208 *BCCI v. Ali* [2000] 3 All ER 51, CA, at [32], [33], [80] and [83].

209 *Statoil ASA v. Louis Dreyfus Energy Services LP* ('*The Harriette N*') [2008] EWHC 2257 (Comm); [2009] 1 All ER (Comm) 1035; [2008] 2 Lloyd's Rep 685.

210 *Ibid.*, at [96].

211 *Ibid.*, at [105].

212 [1986] QB 644, CA.

213 [1986] QB 644 CA; cf *Malcolm v. Chancellor, Masters and Scholars of the University of Oxford* [1994] EMLR 17, CA (publisher's oral assurance that will publish author's work upheld: 4.13).

Unaware of the husband's return to fertility, the couple were lured into an unwanted pregnancy. After the birth, they sued the doctor for the financial cost of bringing up the child. Unable to show negligence on these facts, the claimants based their action on an alleged breach of a contractual guarantee that the operation would be and remain successful. At first instance, they were awarded £10,000 damages.²¹⁴ But a majority of the Court of Appeal (Neill and Nourse LJ, with Kerr LJ dissenting) reversed this, and found in favour of the consultant. The majority decision rests on the objective principle: in their opinion, the doctor's oral assurance was 'mere therapeutic comfort. It was not reasonable that the claimants had been impressed by the doctor's sanguine assurance that the operation would be a success. Nourse LJ observed that 'medicine is not an exact science'.

It would have been different if the claimants had had the wit to ask the consultant doctor at the relevant time: 'Do you really mean that, or are you just offering us well-intentioned reassurance?' If the consultant had responded, 'you can bank on my assurance', or words to that effect, his statement would have lost its quality as 'mere therapeutic comfort'. (Compare the successful claim for strict liability for the accuracy of an express valuation certificate given by a property valuer in *Platform Funding Ltd v. Bank of Scotland plc*, 2009.)²¹⁵

214 In this context in the *tort of negligence*, see now: *McFarlane v. Tayside* [2000] 2 AC 59, HL (and *Parkinson v. St James and Seacroft University Hospital NHS Trust* [2002] 2 QB 266, CA): financial cost of support of child not recoverable, unless child has special needs arising from congenital abnormality, provided not unforeseeable; but damages for pain of pregnancy etc.

215 [2008] EWCA Civ 930; [2009] 2 WLR 1016.

Chapter contents

1. Introduction *para. 4.01*
2. Objective criteria for recognition of contractual rights *para. 4.07*
3. Absence of 'objective criteria' *para. 4.10*
4. Interaction of the 'intent to create legal relations' and 'certainty' doctrines *para. 4.12*
5. Establishing the price in contracts for the sale of goods *para. 4.15*
6. Upholding compromise agreements *para. 4.22*
7. Negotiation exclusively reserved to the parties *para. 4.23*
8. Third party resolution of terms *para. 4.24*
9. No specific performance of vague clauses *para. 4.25*

4

Certainty

1. INTRODUCTION¹

4.01 Summary of main points

Scope of the doctrine of uncertainty

- (1) Problems of 'uncertainty' involve either an initial failure to agree ('vagueness' and 'ambiguity') or a postponement of agreement and eventual failure to agree ('incompleteness').
- (2) Lack of certainty can affect a contract in one of three ways:
 - (a) by invalidating the whole contract;² or
 - (b) by rendering inoperative only part of the contract;³ or
 - (c) by entitling the court to withhold specific performance (a remedy which requires a high degree of precision, because this remedy is ultimately sanctioned by quasi-criminal powers of fines, imprisonment or seizure of assets, under the contempt of court doctrine, 18.13 ff).⁴
- (3) However, uncertainty has no impact on a contract if:
 - (a) the relevant uncertainty leaves a gap which can be filled easily by a statutory or judicial default rule;⁵ or
 - (b) the vague words can be simply ignored, leaving no gap at all.⁶

1 M. Furmston and G. J. Tolhurst, *Contract Formation: Law and Practice* (Oxford, 2010), chapter 11.

2 E.g. *May & Butcher v. R* (1929) [1934] 2 KB 17 n., HL; *Scammell v. Ouston* [1941] AC 251, HL; *British Steel case*, [1984] 1 All ER 504, per Goff J; *Baird Textile Holdings Ltd v. Marks and Spencer plc* [2001] EWCA Civ 274; [2002] 1 All ER (Comm) 737, at [59] to [70], per Mance LJ.

3 See *Didymi Corporation v. Atlantic Lines and Navigation Co. Inc.* [1988] 2 Lloyd's Rep 108, CA (discussed at 4.08).

4 *Co-operative Insurance Society Ltd v. Argyll Stores (Holdings) Ltd* [1998] AC 1, HL; G. H. Jones, [1997] CLJ 488-91; A. M. Tettenborn, [1998] Conv 23.

5 E.g. section 8(2) of the Sale of Goods Act 1979, imposing reasonable price if a contract for the sale of goods does not specify a price: 4.16.

6 *Nicolene Ltd v. Simonds* [1953] 1 QB 543, CA (uncertain language ignored; remainder upheld).

Judicial desire to uphold various types of bargain

- (4) Agreement on essential terms normally suffices, because the courts or the relevant statutory framework can fill any gap.⁷ For example, in a sale of goods, essential matters are confined to the subject matter of the sale, since the price can be implied by law (provided the parties are silent on the price). The price, if left open, *can* be implied by section 8 of the Sale of Goods Act 1979 (4.15 ff).
- (5) The courts strive to resolve problems of uncertainty in favour of finding an agreement.
- (6) The courts are especially keen to find an agreement when there has been significant performance under a purported agreement.
- (7) The parties can stipulate that a third party (or set of third parties) can fill a blank (for example, fix the price). If so, the courts might regard this as inessential machinery. But it is a question of construction, assessed by reference to the commercial context, whether the third party resolution is essential to the parties' relations. If it is, the court cannot substitute its own objective determination (4.24).
- (8) Contracts of compromise, where court litigation has been contemplated or already commenced, are especially likely to be upheld, even if the agreement reveals elements of uncertainty. In *Scammell v. Dicker* (2005),⁸ Rix LJ emphasised the need for consent orders of this type to be upheld, especially when the order has already caused legal proceedings to be terminated and there has been a significant passage of time before the challenge to the order's validity.⁹

Overlap with intent to create legal relations

- (9) The less precise an agreement is, the greater the chance that the courts will conclude that the parties had no real intention to conclude a legally binding agreement (on intent to create legal relations, see chapter 6).

Reserving the right to autonomous negotiation ('freedom of contract')

- (10) The courts will not override the negotiating parties' clear reservation of the right to negotiate terms or a particular term. The principle of 'freedom of contract' (1.08) will then preclude the courts from imposing a contract (4.06). But restitutionary relief might be available if goods have been delivered or services performed.

⁷ *May & Butcher v. R* [1934] 2 KB 17, 22, HL, *per* Lord Warrington; *Scammell v. Dicker* [2005] 3 All ER 838, CA, at [40] (third sentence from end), *per* Rix LJ.

⁸ [2005] EWCA Civ 405; [2005] 3 All ER 838.

⁹ *Ibid.*, at [39], [40] and [42].

- 4.02 *Need for objective guidelines for adjudication.* The law of ‘certainty’ is largely the task of determining the practical limits of contractual adjudication over disputes concerning the breakdown of consensus (although largely a matter of practicality, the topic of uncertainty also involves a point of principle, namely, the reservation by the parties of a central issue for negotiation, 4.06).
- 4.03 The need for adjudicative standards for dispute resolution explains why agreements to agree (2.07) are treated as too vague to receive legal force: there are not enough pointers to guide and regulate reliable decision-making by the courts (or by arbitrators).¹⁰ The courts have prudently avoided the high risk that adjudicators would become embroiled in the hopeless task of assessing the fairness or reasonableness of each party’s bargaining steps. We have seen that an agreement to negotiate in good faith or reasonably is void for uncertainty (2.07).¹¹ By contrast, when determining whether a party has taken adequate steps to procure the third party’s permission, there are sufficient commercial and objective guidelines to enable the courts to reach a satisfactory answer to such a dispute. In this latter context, the relevant party is making a commitment to try to attain a specific goal (2.10). Whether he has failed to take adequate steps to achieve it is a commercial matter open to objective determination by the courts. The line is drawn, therefore, between open-ended declarations of intent to negotiate the terms of the proposed main contract and a more specific undertaking to obtain from a third party a ‘green light’ necessary for the main contract. More generally, Sir Andrew Morritt V-C in *Baird Textile Holdings Ltd v. Marks and Spencer plc* (2001)¹² spelt out the need for objectivity, referring to ‘cases where the contract provides for an objective standard which the court applies by ascertaining what is reasonable’, as distinct from illegitimately imposing a contract on the parties where they have reserved to themselves the task of negotiating from rival positions (and see the cases examined at 2.11). In *Phillips v. Enron* (1997), during discussion of a ‘reasonable endeavours’ clause, Potter LJ also explained the need for objective criteria:¹³

[T]he unwillingness of the courts to give binding force to an obligation to use ‘reasonable endeavours’ to agree seems to me to be sensibly based on the difficulty of policing such an obligation, in the sense of drawing the line between what is to be regarded as reasonable or unreasonable in an area where the parties may legitimately have differing views or interests, but have not provided for any criteria on the basis of which a third party can assess or adjudicate the matter in the event of dispute. In the face of such difficulty, the court does not give a remedy to a party who may with justification assert, ‘well, whatever the criteria are, there must have been a breach in this case’. It denies the remedy altogether on the basis of the unenforceability in principle of an obligation which may fall to be applied across a wide spectrum of

10 *Walford v. Miles* [1992] 2 AC 128, HL; and *Little v. Courage* (1995) 70 P & CR 469, CA.

11 Acknowledged in *Walford v. Miles* [1992] 2 AC 128, HL.

12 [2001] EWCA Civ 274; [2002] 1 All ER (Comm) 737, at [26].

13 [1997] CLC 329, 343, CA; also, at 339, explaining *Queensland Electricity Generating Board v. New Hope Collieries* [1989] 1 Lloyd’s Rep 205, PC, on this basis: 2.08.

arguable circumstances ... In all those respects, the [negotiation clause in this case] utterly fails to reveal any express or implied criteria to be applied.

4.04 *Agreement already substantially settled.* Secondly, the courts recognise the practical need to facilitate an agreement once its terms have been substantially settled: see the instructive remarks – too long to cite here – of Neuberger J in *Liverpool City Council v. Walton* (2001).¹⁴

4.05 *Supposed agreement already partly performed.* This leads to another theme in this area of contract law, the question of part-performance: the courts are especially willing to overcome problems of suggested uncertainty if the parties have conducted themselves in a manner which suggests that they had assumed that a binding transaction has arisen. On this point, Lord Steyn, echoing several leading judicial statements,¹⁵ has written:¹⁶

The reasonable expectations of the parties, albeit that they are still in disagreement about minor details of the transaction, often demand that the court must recognise that a contract has come into existence. The greater the evidence of reliance, and the further along the road towards implementation the transaction is, the greater the prospect that the court will find a contract made and do its best, in accordance with the reasonable expectations of the parties, to spell out the terms of the contract.

4.06 *Parties' reservation of right to determine the agreement.* The negotiating parties might postpone the legal operation of their proposed transaction until they have themselves (without outside interference or extraneous reference) settled its various aspects. The principle of 'freedom of contract' (1.08) requires the courts to respect this autonomous zone of private negotiation. For example, negotiating parties might have reserved exclusively to themselves the task of agreeing the price in a contract for the sale of goods. In default of agreement, they might have (expressly or impliedly) barred any form of outside determination of that price. Such a joint veto on contractual enforcement can only be lifted if both parties consent. However, as a matter of practical justice, this can be inconvenient: if the goods are in the meantime delivered, the courts cannot find a contract in order to justify imposing a reasonable price for the goods. All that can be done is to impose on the recipient a *non-contractual* duty to pay a reasonable sum for the goods (based on the law of restitution). But this is a one-sided solution: the recipient of the goods must pay, but he has no contractual rights to complain of bad delivery, for example, slow and muddled delivery of building materials (as in the *British Steel* case (1984),¹⁷ 2.04).

14 [2002] 1 EGLR 149; [2001] NPC 135, at [49] to [54] (the case was argued by two eminent QCs, Derek Wood and Kim Lewison).

15 Proposition affirmed in *Scammell v. Dicker* [2005] 3 All ER 838, CA, at [31]; and *per* Lord Tomlin in the *Hillas* case (1932) 147 LT 503, 512, HL; and *per* Steyn LJ in *Trentham Ltd v. Archital Luxfer Ltd* [1993] 1 Lloyd's Rep 25, 27, CA.

16 Lord Steyn, 'Contract Law: Fulfilling the Reasonable Expectations of Honest Men' (1997) 113 LQR 433, 435, echoing his decision in the *Trentham* case (see the previous note).

17 [1984] 1 All ER 504, Goff J.

2. OBJECTIVE CRITERIA FOR RECOGNITION OF CONTRACTUAL RIGHTS

- 4.07 The House of Lords found an objective yardstick in *Hillas & Co. v. Arcos Ltd* (1932) and so was able to uphold a contract on these facts.¹⁸

In 1930, the parties contracted that the defendants would sell to the claimant at an agreed price 22,000 'standards' of Russian 'softwood goods of fair specification'. There was an option allowing the claimant to purchase 100,000 timber standards for delivery during 1931. Although the option specified the price adequately, there was a dispute whether it also provided adequate certainty concerning its subject matter, notably the timber's size and quality. But the House of Lords held that these problems melted away if the 1931 option were construed by objective reference to the criterion of a 'fair specification' contained in the 1930 agreement. This was a clear enough yardstick. It would enable the court to control the vendor's delivery of timber during 1931, once the option was exercised by the purchaser. Lord Thankerton said:¹⁹ '[T]he contract is a commercial one and ... the parties undoubtedly thought that they had concluded a contract; and I have come to the conclusion ... that there was here a concluded contract.'

The Court of Appeal in *Durham Tees Valley Airport Ltd v. bmibaby Ltd* (2010)²⁰ applied the *Hillas* case:

The Court of Appeal held that the defendant's agreement to run a low-cost flight service at the claimant's airport for a period of ten years by 'establishing a 2 based aircraft operation' was not void for uncertainty. Accordingly, damages could be awarded for the airline's failure to adhere to this undertaking. Patten LJ said:

[A.] Many of the cases in which this issue has arisen involve contracts for the supply of goods where either quantity, quality or price is expressed in non-specific terms. In *Hillas & Co. Ltd v. Arcos Ltd* itself the timber sold was to be 'of fair specification'. The court's attitude has been to attempt to give effect to the contract by resorting to market rates and prices or to trade standards which provide objective criteria for the determination of what the parties agreed.

[B.] Where such criteria exist and are ascertainable then a term of reasonableness is often implied in order to incorporate them as the measure of performance required under the contract. This is no more than part of the process of construction which the court is required to undertake.

As for proposition B, the court held that no implied terms needed to be found in this case to supplement the express terms of the contract. Even though those terms were scanty, they were enough to disclose a binding contract, which the defendant had clearly repudiated. Toulson LJ said:²¹

18 (1932) 147 LT 503; [1932] All ER 494, HL; Lord Thankerton's reference to an 'objective yardstick' was cited by Sir Andrew Morritt V-C in *Baird Textile Holdings Ltd v. Marks and Spencer plc* [2001] EWCA Civ 274; [2002] 1 All ER (Comm) 737, at [26] to [30] (generally on the latter case, see 6.13).

19 [1932] All ER 494, 502, HL.

20 [2010] EWCA Civ 485.

21 *Ibid.*, at [91].

It is not uncommon in commercial life for parties to enter into a contract by which one party is to conduct an operation over which it has a large degree of discretion; but it will usually be possible for a court to determine without too much difficulty whether that party has ceased to perform the operation at all. The present contract may be unusual in its length and the degree of discretion given to the airline, but I do not see that the court would have an insuperable difficulty in deciding whether the airline had altogether ceased to conduct the operation.

Finally, as Patten LJ explained, damages could be awarded on the following basis (see also 18.23):²²

The court has to look at the relevant economic and other surrounding circumstances to decide on the level of performance which the defendant would have adopted. The judge conducting the assessment must assume that the defendant would not have acted outside the terms of the contract and would have performed it in his own interests having regard to the relevant factors prevailing at the time. But the court is not required to make assumptions that the defaulting party would have acted uncommercially merely in order to spite the claimant.

- 4.08 *Hire rate to be 'equitably' adjusted under a charterparty.* The Court of Appeal's decision in *Didymi Corporation v. Atlantic Lines and Navigation Co. Inc.* (1988) shows that a clause will be upheld if there is some objective yardstick, even if not immediately transparent, against which the court can regulate the parties' entitlement and obligations.²³

The case concerned a charterparty for five years. The basic rate of hire was agreed. But the contract further provided that this sum could be raised or reduced to reflect the ship's speed and efficiency. The relevant clause provided that adjustment should be 'mutually agreed' according to what was 'equitable'. The owners claimed such an increase. The hirer said that the variation clause was void. The Court of Appeal, somewhat optimistically, regarded the word 'equitable' as a clear enough criterion to permit objective assessment of the disputed hire payment.

The case was distinguished by the Court of Appeal in *Phillips Petroleum Co. (UK) Ltd v. Enron (Europe) Ltd* (1999), which concerned a commercial undertaking to exercise reasonable endeavours to negotiate terms within an existing agreement, and where no objective criterion had been stated, nor could one be safely implied: 2.11.²⁴

22 *Ibid.*, at [79], *per* Patten LJ (Toulson and Mummery LJJs agreed: *ibid.*, at [147] and [150]), considering, notably, *Abrahams v. Herbert Reich Ltd* [1922] 1 KB 477, CA (preferring the approach of Atkin LJ to that of Scrutton LJ); *Lavarack v. Woods of Colchester* [1967] 1 QB 278, CA; *Paula Lee Ltd v. Zehil & Co. Ltd* [1983] 2 All ER 390, Mustill J; *Kurt A Becher GmbH & Co. KG v. Roplak Enterprises SA ('The World Navigator')* [1991] 2 Lloyd's Rep 23, CA; *Cantor Fitzgerald International v. Horkulak* [2004] EWCA Civ 1287; [2005] ICR 402.

23 [1988] 2 Lloyd's Rep 108, CA (noted by Reynolds, (1988) 104 LQR 353), considering (1) *Sudbrook Trading Estate Ltd v. Eggleton* [1983] 1 AC 444, HL, and *Brown v. Gould* [1972] Ch 53, Megarry J (both contracts certain), and (2) *Courtney v. Tolaini* [1975] 1 WLR 297, CA and *Mallozzi v. Carapelli SpA* [1976] 1 Lloyd's Rep 407, CA (both contracts uncertain).

24 [1996] EWCA Civ 693; [1997] CLC 329, 343–4, *per* Potter LJ.

- 4.09 How wide is the *Didymi* case's authority? There are two points. First, it is probably important that the other terms in this contract were unproblematic and that the contract had already lasted for a significant period before the disputed issue arose (for a similar point, see the *Foley* case at 4.20). Secondly, although the *Didymi* decision upholds the word 'equitable' in that particular commercial context (efficiency of a chartered vessel's sailing performance), the same word might not possess sufficient certainty in all other contexts. The criterion of what is 'equitable', which is merely a synonym for 'fair', must be capable of reasonably straightforward application in the relevant context. Where the context involves assessment of subjective matters, such a formula would prove unworkable. For example, an agreement for the 'equitable' award of a specified bonus fee to a lecturer to reflect students' appreciation of a particular course would not be certain enough. It would be different if the agreement more explicitly stated: 'if a majority of the "feedback" returns record satisfaction greater than seven out of ten marks'.

The decision in the *Didymi* case can be contrasted with *Gillatt v. Sky Television Ltd* (2000),²⁵ where the Court of Appeal held that a stipulation for valuation (the clause contemplated that this would be effected by an independent valuer) 'of the open market value' of shares in a private company did not disclose any objective means of determining which method of valuation should be adopted. The court was informed that private company shares are capable of being valued on various 'bases': asset value, earnings, discounted cash flow, or a combination of these (for more on this case, see 4.24). In the face of this variety of methods, and in default of an independent valuation, the court considered that it would be out of its depth and all at sea.

3. ABSENCE OF 'OBJECTIVE CRITERIA'

- 4.10 *Hopeless ambiguity in description of goods.* *Raffles v. Wichelhaus* (1864)²⁶ is the leading authority on a type of written contract where 'latent ambiguity' *might* render the apparent agreement void for uncertainty.

This case concerned a supposed contract for the purchase of a cargo of 'cotton ex Peerless' from Bombay for delivery at Liverpool. It turned out that there were two ships called 'Peerless': one was leaving Bombay in October, the other in December, in the same year; but both ships were to bring cotton to Liverpool from Bombay. The buyer refused to accept delivery of cotton from the December ship, and instead alleged that he had intended cotton from the October ship. The seller sued for non-payment of the price in respect of the December cargo. The action could not immediately succeed because the courts could not discern to which vessel the supposed contract was referring. The preliminary question was whether the buyer could adduce extrinsic evidence (evidence outside the text of the agreement) to show that there was such an ambiguity. Unfortunately, the court did not give a reasoned decision, but

²⁵ [2000] 1 All ER (Comm) 461, CA.

²⁶ (1864) 2 H & C 906; G. Gilmore, *The Death of Contract* (Columbus, OH, 1974), 35–44; A. W. B. Simpson, *Leading Cases in the Common Law* (Oxford, 1995), 135 ff.

simply stopped counsel during argument and declared that judgment should be entered for the defendant buyer.

In other words, the decision on this preliminary issue was that the case must proceed to the jury (this form of adjudication was still common in the nineteenth century, but has ceased to apply in modern contract law) to determine on the facts whether the parties were truly at cross-purposes; if so, the contract would be void; conversely, if the jury decided that the seller's version should be upheld, the buyer would be liable to pay the price claimed. Perhaps it would prove impossible to resolve this impasse on the facts, since both versions were equally 'reasonable'. The result of the further proceedings is not recorded.

Chitty notes that it would be unlikely that in modern conditions a contract would be as sparsely worded as this and thus fail to provide any objective clue as to its true subject matter.²⁷

- 4.11 *Hire-purchase: subject matter.* In *Scammell v. Ouston* (1941),²⁸ the House of Lords held that it could not discern a clear enough transaction, only the shadowy beginnings of a real contract. And so the arrangement was void.

This was an intended sale of a lorry in part-exchange for an old one. The transaction was made 'on the understanding that the balance of the purchase price can be had on hire-purchase terms over a period of two years'. The vendor refused to deliver. The House of Lords held that this transaction was irredeemably vague and thus a nullity. Viscount Maugham explained that (in the early 1940s) hire-purchase agreements were novel and unfamiliar, and that there were different forms of hire-purchase. For these reasons, terms could not be securely implied:²⁹

[N]othing is said (except as to the two years period) as to the terms of the hire-purchase agreement, for instance, as to the interest payable, and as to the rights of the [owner] ... in the event of default by the respondents in payment of the instalments at the due dates. As regards the last matters there was no evidence to suggest that there are any well known 'usual terms' in such a contract.

4. INTERACTION OF THE 'INTENT TO CREATE LEGAL RELATIONS' AND 'CERTAINTY' DOCTRINES³⁰

- 4.12 *Vague publishing contract.* The vaguer the suggested agreement, especially in a context where precision and detail are normally to be expected, the less likely it will be that the court will infer that the negotiating parties had reached an immediate agreement, intending to give it legal force (generally on the doctrine of 'intent to create legal relations', see chapter 6). As Mustill LJ noted in *Malcolm v. Chancellor, Masters and Scholars of the University*

²⁷ *Chitty on Contracts* (30th edn, London 2008), 5-071.

²⁸ [1941] AC 251, HL.

²⁹ *Ibid.*, at 256-7.

³⁰ On the 'intent to create legal relations' doctrine, see chapter 6.

of *Oxford* (1994),³¹ 'the first question must always be whether any legally binding contract has been made'. The court should not prejudge this question by first constructing an agreement from a set of implied terms and then declare that the parties must have reached an agreement. However, as we shall see in the next paragraph, the majority's decision in that case (in which Mustill LJ dissented) is at the extreme limits of acceptable certainty.

- 4.13 The decision in the *Malcolm* case (1994)³² is a rather extreme example of the courts heroically filling in large gaps in an oral agreement to publish a book. It is also a 'David and Goliath' case because Malcolm represented himself in the Court of Appeal, where he was victorious in establishing a valid agreement. The problem had arisen from these facts.

During a telephone conversation between Malcolm, author of a philosophical treatise, and a senior editor of Oxford University Press (OUP), the latter seemed to have indicated that the Press would definitely publish Malcolm's book: 'I am pleased that we are going to do your book', he said, and added at 'a fair royalty'. The editor was later disciplined for these casual and fateful remarks. In due course, OUP's Delegates (the decision-making board for proposed new publications) decided that the book was unsuitable for OUP. Malcolm sought specific performance of the oral undertaking. The claim failed at first instance, the judge deciding that there was no contract because the oral undertaking was too vague and incomplete.

But a majority of the Court of Appeal reversed this (Nourse and Leggatt LJ; for the dissent by Mustill LJ, see 4.14). They regarded this exiguous oral undertaking as sufficiently certain. In their opinion, in default of agreement, a fair royalty could be worked out by the court (the standard range of royalty offered by law book publishers in the United Kingdom is 10–15 per cent on cover price sales; whether or not this range is 'fair', it would probably be adopted by the court). Nor was it fatal that OUP had not agreed the print run of the book. Nor did it matter that the parties had not decided whether the book would be in hardback. Such uncertainties could be resolved by the publisher exercising its commercial judgment.

Although Malcolm succeeded in establishing a contract on these facts, he did not obtain his preferred remedy. Specific performance was denied. Specific performance (18.14) to compel a publisher to publish a book is possible; but not automatic; the court has a discretion. At first instance, Lightman QC, the deputy High Court judge, in a *dictum*, had said that on the present facts he would have exercised his discretion so as to withhold specific performance. The Court of Appeal endorsed this.

Instead, the Court of Appeal awarded damages. Assessment of that compensation was then remitted to the court at first instance.³³

31 [1994] EMLR 17, CA, citing *Aoterroa International Scancarriers* [1985] 1 NZLR 513, PC; for an excellent example, see 6.13 on *Baird v. Marks and Spencer plc* [2001] EWCA Civ 274; [2002] 1 All ER (Comm) 737.

32 [1994] EMLR 17, CA.

33 On the inquiry as to damages, [2002] EWHC 10; [2002] EMLR 277; Malcolm published an account of the saga: A. Malcolm, *The Remedy* (Brighton, 1997).

- 4.14 Mustill LJ dissented in the *Malcolm* case (4.13). He regarded the editor's telephone assurance as a mere 'gentlemen's agreement'. In his opinion, as a matter of objective construction of the telephone conversation, the editor's assurance was not intended to create legal relations. There is much sense in this dissent. The majority decision is very odd. For everyone knows that in practice a publishing contract (in England, as distinct from Japan, or even Germany) is many pages long, loaded in favour of the publisher's standard terms, and that the custom is that it should be signed by both parties. A reasonable person – even a very abstract philosopher – would not rely on vague undertakings to publish expressed on the phone. Instead, a 'streetwise' author would know that a signed publishing contract would be the earliest point at which a solid agreement would arise.³⁴

5. ESTABLISHING THE PRICE IN CONTRACTS FOR THE SALE OF GOODS

- 4.15 As mentioned in the introduction (4.01), the courts will often strain to find a contract if at least one of the parties has begun to perform a supposed transaction. This tendency is illustrated by cases concerning the ascertainment of the price in contracts for the sale of goods.
- 4.16 Let us begin by noting the four rules governing the ascertaining of the price in contracts for the sale of goods:
- (1) The Sale of Goods Act 1979 (SGA 1979) will impose a reasonable price if the parties have simply left the matter of price as a blank item. This default rule is contained in section 8, which states:
 - (a) The price in a contract of sale may be fixed by the contract, or may be *left to be fixed in a manner agreed by the contract*, or may be determined by the course of dealing between the parties.
 - (b) Where the price is not determined as mentioned in subsection (1) above the buyer must pay the reasonable price.
 - (c) What is a reasonable price is a question of fact dependent on the circumstances of each particular case.
 - (2) If the price is fixed by reference to some ascertainable price register, the contract will be upheld by ascertaining the relevant figure. This follows from the wording of section 8(1) where it states that the price 'may be left to be fixed in a manner agreed by the contract'.
 - (3) If the price is to be fixed by a panel of valuers, but one party fails to co-operate in the appointment of the valuers, section 9(2) SGA 1979 renders the party at fault liable for damages³⁵ (generally on the issue of third party resolution, see 4.24).

³⁴ Cf consultant doctor's assurance not a contractual guarantee: *Thake v. Maurice* [1986] QB 644, CA: see 3.71.

³⁵ The 1979 Act uses the remedy of damages; cf *Sudbrook Trading Estate v. Eggleton* [1983] 1 AC 444, HL (party frustrating an agreement that each side should appoint valuers to determine the price concerning a proposed sale of *land*; specific performance to compel the grant of a lease at a fair valuation).

- (4) Where there has been no performance (a situation known as an ‘executory’ sale of goods), the contract might be void for incompleteness. Section 8 SGA 1979 will not supply the ‘reasonable price’ if the parties have expressly left the price open saying ‘at a price to be agreed’ and there is no default provision such as reference of the price to a third party valuer (see the next paragraph).

4.17 The leading case concerning situation (4) above is *May & Butcher v. R* (1929).³⁶

The relevant clause referred to the purchase of old tentage, ‘the price or prices to be paid ... shall be agreed from time to time between [the parties]’. The House of Lords (in a decision not reported until 1934) held that there was no contract on these facts. The contract was not simply silent on the question of price: instead, the matter had been left for determination by the parties, without specific recourse to a ‘fall-back’ if they should fail to agree. Although the arrangement was subject to an arbitration clause, the House of Lords held that this did not alter the analysis. The arbitration clause clothed the arbitrator with power to determine matters ‘with reference to or arising out of this agreement’. But that last phrase begged the question whether there was in fact a valid contract. On this last point, Lord Buckmaster said: ‘The arbitration clause relates to the settlement of whatever may happen when the agreement has been completed and the parties are regularly bound. There is nothing in the arbitration clause to enable a contract to be made which in fact the original bargain has left quite open.’³⁷ Viscount Dunedin decided this aspect of the case by reference to a distinction between a disagreement and a dispute, a distinction now regarded as sterile and unconvincing. He said: ‘In no proper meaning of the word can this be described as a dispute arising between the parties; it is a failure to agree, which is a very different thing from a dispute.’³⁸

4.18 *May & Butcher v. R* (1929) has been criticised by the New Zealand Court of Appeal in *Electricity Corporation of New Zealand Ltd v. Fletcher Challenge Ltd* (2001), especially in light of the fact that there had been an arbitration clause.³⁹

We find curious the notion that, in a commercial contract where price is left to be agreed, a reasonable price cannot be fixed and that, even where there is an arbitration clause, that clause cannot be used to determine the price because ‘unless the price has been fixed, the agreement is not there’ ... We agree with Professor McLauchlan, ‘Rethinking Agreements to Agree’ (1998) 18 NZULR 77, 85, that ‘an agreement to agree will not be held void for uncertainty if the parties have provided a workable formula or objective standard or a machinery (such as arbitration) for determining the matter which has been left open’. We also agree with him that the court can step in and apply the formula or standard if the parties fail to agree or can substitute other machinery if the designated machinery breaks down.

³⁶ [1934] 2 KB 17 n., HL.

³⁷ *Ibid.*, at 21.

³⁸ *Ibid.*

³⁹ [2001] NZCA 289; [2002] 2 NZLR 433, at [61] and [62].

If this point were to recur in England, one possible construction of an arbitration clause similar to that in the *May & Butcher* case would be that the parties had intended that the arbitrator should fix a (reasonable) price in the absence of the parties' agreement on that aspect. The modern law supports this approach. First, the (English) Arbitration Act 1996 defines an arbitration clause as covering both 'disputes' and 'differences' (agreements 'to submit to arbitration present or future disputes, whether they are contractual or not',⁴⁰ and this includes 'any difference').⁴¹ Furthermore, it is now clear that an arbitration clause can subsist even if the main contract is *prima facie* invalid. Thus, section 7 of the Arbitration Act 1996 provides that an arbitration clause can be valid even though the arbitration will determine whether the main contract is valid or not:

Unless otherwise agreed by the parties, an arbitration agreement which forms or was intended to form part of another agreement (whether or not in writing) shall not be regarded as invalid, non-existent or ineffective because that other agreement is invalid, or did not come into existence or has become ineffective, and it shall for that purpose be treated as a distinct agreement.

In the *Premium Nafta Products* case (2007), Lord Hoffmann has explained:

[Section 7 of the Arbitration Act 1996] shows a recognition by Parliament that ... businessmen frequently do want the question of whether their contract was valid, or came into existence, or has become ineffective, submitted to arbitration and that the law should not place conceptual obstacles in their way.⁴²

He added:

Of course there may be cases in which the ground upon which the main agreement is invalid is identical with the ground upon which the arbitration agreement is invalid. For example, if the main agreement and the arbitration agreement are contained in the same document and one of the parties claims that he never agreed to anything in the document and that his signature was forged.⁴³

Furthermore, the court went on to hold that arbitration clauses are nowadays to be construed in a liberal fashion.⁴⁴ Lord Hoffmann said:

40 Section 6(1) of the Arbitration Act 1996.

41 *Ibid.*, section 82(1); M. Mustill and S. Boyd, *Commercial Arbitration: Companion Volume* (London, 2001), 22–3; *Hayter v. Nelson and Home Insurance* [1990] 2 Lloyd's Rep 265; the Departmental Advisory Committee's February 1996 Report at [41], explains that 'difference' was added to widen the definition (following (FG) *Sykes v. Fine Fare Ltd* [1967] 1 Lloyd's Rep 53, 60; noted in M. Mustill and S. Boyd, *Commercial Arbitration* (2nd edn, London, 1989), 128 n. 17).

42 *Premium Nafta Products Ltd v. Fili Shipping Co. Ltd* (otherwise known as the *Fiona Trust* case) [2007] UKHL 40; [2007] 4 All ER 951, at [10] (noted by L. Flannery, (2007) NLJ 1756; A. Rushworth, (2008) 124 LQR 195; A. Briggs, [2008] LMCLQ 1).

43 *Ibid.*, at [17] to [19]; e.g. *Albon v. Naza Motor Trading Sdn Bhd* [2007] EWCA Civ 1124; [2008] 1 Lloyd's Rep 1 (forged signature upon main agreement and arbitration clause; High Court determining both issues).

44 *Premium Nafta Products Ltd v. Fili Shipping Co. Ltd* [2007] UKHL 40; [2007] 4 All ER 951.

[T]he construction of an arbitration clause should start from the assumption that the parties, as rational businessmen, are likely to have intended any dispute arising out of the relationship into which they have entered or purported to enter to be decided by the same tribunal. The clause should be construed in accordance with this presumption unless the language makes it clear that certain questions were intended to be excluded from the arbitrator's jurisdiction.

4.19 In conclusion on the troublesome *May & Butcher* case, two points can be made. First, one feature of the case, not emphasised in the decision, has since gained great prominence: there had been no performance on either side in *May & Butcher*. This aspect becomes relevant when the *Foley* case (1934) is considered in the next paragraph. The second point is that it is unclear whether the same result would now be reached in the *May & Butcher* case in view of the liberal approach now adopted concerning arbitration clauses ancillary to valid or purported contracts (4.18). The result in *May & Butcher* might be defended only if the main agreement were interpreted as a situation where, in default of their own determination of a vital term, the parties were unwilling to have the price determined by reference to an outsider (if so, the case would be similar to *Courtney & Fairbairn Ltd v. Tolaini Bros (Hotels) Ltd* (1975), 4.23). That was the analysis adopted in *May & Butcher* by Lord Warrington:⁴⁵ '[T]o apply the arbitration clause would be, as in the attempted application of the doctrine as to reasonable price, to substitute the award of the arbitrator for that agreement between the parties which was the term by which they had originally agreed to be bound.' But the opposite view is distinctly arguable: that, under current law, inclusion of an arbitration clause is intended to cut the Gordian knot if it should happen that the parties either dispute whether they have agreed a price, or there is a failure to agree (and see, for support, the passage cited from the *Mamidoil-Jetoil* case (2001)⁴⁶ at 4.20). In either situation, a 'difference' or 'dispute' has arisen concerning the fixing of a price. The arbitration agreement can be interpreted as concerned to resolve that impasse. And this might be regarded as consistent with section 8(1) of the Sale of Goods Act 1979, which states, *inter alia*: 'The price in a contract of sale ... may be left to be fixed in a manner agreed by the contract ...'. The argument that the arbitration agreement cannot subsist unless and until the main agreement is activated melts away: section 7 of the Arbitration Act 1996 (4.18) renders the validity of the arbitration clause independent of the validity of (or currently inoperative status of) the main agreement.

4.20 *Substantial dealings under a contract for regular supply of goods.* It appears that a contract of sale will not be regarded as void for incompleteness if the goods have been delivered and accepted. In *Foley v. Classique Coaches* (1934),⁴⁷ the Court of Appeal distinguished the House of Lords decision in *May & Butcher v. R* (1929) (4.17 to 4.19) as concerned with a contract where no delivery or deliveries had occurred.⁴⁸ In the *Foley*

⁴⁵ [1934] 2 KB 17 n. at 22, HL.

⁴⁶ *Mamidoil-Jetoil Greek Petroleum Co. Ltd v. Okta Crude Oil Refinery (No. 1)* [2001] EWCA Civ 406; [2001] 2 Lloyd's Rep 76, at [69].

⁴⁷ [1934] 2 KB 1, CA.

⁴⁸ The House of Lords approved the *Foley* case in *Scammell v. Ouston* [1941] AC 251.

case, the court found an implied term that, if the parties failed to agree the price, a reasonable sum should be imposed, this sum to be fixed by the arbitrator (the contract included an arbitration clause).

The *Foley* case concerned an agreement for the exclusive purchase of petrol by the defendant from the claimant 'at a price to be agreed by the parties in writing from time to time'. The defendant ran a coach business. The defendant bought petrol from the claimant for roughly three years at prices below the retail level. Then the defendant considered it could obtain 'better' petrol from elsewhere. So it contended that there was no real agreement, merely an agreement to agree, so that the supposed contract for exclusive purchase had all along been void for uncertainty. The Court of Appeal, affirming the trial judge (Lord Hewart CJ), rejected that argument. It held that there was an implied term that, if the parties failed to agree the price, a reasonable sum should be imposed by the arbitrator.

It is notable that the arrangement had already operated for three years. This was in contrast to the executory agreement in *May & Butcher*. Another factor supporting the result was that the petrol supply agreement contained an arbitration clause to cover disputes, including failure to agree on the price of petrol, although the arbitration agreement was perhaps not decisive. Yet another supporting factor was that the claimant had insisted on the supply contract being signed before selling some land to the defendant.

In the *Foley* case Scrutton LJ explained:⁴⁹

[T]he parties obviously believed they had a contract and they acted for three years as if they had; they had an arbitration clause which relates to the subject matter of the agreement as to the supply of petrol, and it seems to me that this arbitration clause⁵⁰ applies to any failure to agree as to the price ... There is to be implied in this contract a term that the petrol shall be supplied at a reasonable price and shall be of reasonable quality. For these reasons ... there was an effective and enforceable contract, although as to the future no definite price had been agreed with regard to the petrol.

In *Beer v. Bowden* (1981), Goff LJ held that the *Foley* case did not turn on the existence of an arbitration clause.⁵¹ Instead, he interpreted its *ratio* as the implication *by the court (without the need for arbitration)* of a reasonable price, if the parties failed to agree upon a price. The *Foley* case can be interpreted as permitting the court to impose a reasonable price where there has been a supply and consumption of goods, even though the contract expressly left the price to be agreed. The *Foley* decision's finding of an agreement avoids the one-sided restitutionary analysis of the *British Steel* case (1984)⁵² (2.04), the supplier gaining payment but the recipient having no counter-claim for unsatisfactory performance. It is submitted that English law should, and probably already does, recognise a

49 [1934] 2 KB 1, 9–10, CA.

50 *Beer v. Bowden* [1981] 1 WLR 522, 526, CA, *per* Goff LJ, absence of an arbitration clause not conclusive.

51 *Ibid.*

52 [1984] 1 All ER 504, 510F–511F, Goff J.

principle that performance can override the absence of a clear consensus, even on a fundamental matter such as price.⁵³ The parties' conduct, especially if there has been consistent dealing, supports a finding that there is a contract. The only settled exception is where the parties' performance has been expressly designated as 'subject to contract' (12.04; also 1.16, 2.07, 4.21, 6.06). This formula normally precludes contractual rights; although, exceptionally, as the Supreme Court's decision in *RTS Flexible Systems Ltd v. Molkerei Alois Müller GmbH* (2010)⁵⁴ (4.21) shows, the courts can infer that the parties impliedly agreed to waive that formula, provided the parties have resolved all key points of difference during their negotiations.

These threads have been attractively woven by Rix LJ in the *Mamidoil-Jetoil* case (2001) into this general statement:⁵⁵

In my judgment the following principles [emerge from the earlier cases], but this is intended to be in no way an exhaustive list:

- i) Each case must be decided on its own facts and on the construction of its own agreement. Subject to that,
- ii) Where no contract exists, the use of an expression such as 'to be agreed' in relation to an essential term is likely to prevent any contract coming into existence, on the ground of uncertainty. This may be summed up by the principle that 'you cannot agree to agree'.
- iii) Similarly, where no contract exists, the absence of agreement on essential terms of the agreement may prevent any contract coming into existence, again on the ground of uncertainty.
- iv) However, particularly in commercial dealings between parties who are familiar with the trade in question, and particularly where the parties have acted in the belief that they had a binding contract, the courts are willing to imply terms, where that is possible, to enable the contract to be carried out.
- v) Where a contract has once come into existence, even the expression 'to be agreed' in relation to future executory obligations is not necessarily fatal to its continued existence.
- vi) Particularly in the case of contracts for future performance over a period, where the parties may desire or need to leave matters to be adjusted in the working out of their contract, the courts will assist the parties to do so, so as to preserve rather than destroy bargains, on the basis that what can be made certain is itself certain. *Certum est quod certum reddi potest.*

53 *Atiyah's Sale of Goods* (12th edn, London, 2010), 30–1: courts should fix a reasonable price in any contract of sale containing an agreement to agree the price, where the parties have partly performed the contract; similarly, M. Bridge, *The Sale of Goods* (2nd edn, Oxford, 2009), 1.42 ff (citing also Rix LJ's general statement in *Mamidoil-Jetoil Greek Petroleum Co. Ltd v. Okta Crude Oil Refinery (No. 1)* [2001] EWCA Civ 406; [2001] 2 Lloyd's Rep 76, at [69], passage cited in text below); *Benjamin on Sale* (7th edn, London, 2006), 2–046, is slightly more cautious.

54 [2010] UKSC 14; [2010] 1 WLR 753.

55 *Mamidoil-Jetoil Greek Petroleum Co. Ltd v. Okta Crude Oil Refinery (No. 1)* [2001] EWCA Civ 406; [2001] 2 Lloyd's Rep 76, at [69].

- vii) This is particularly the case where one party has either already had the advantage of some performance which reflects the parties' agreement on a long term relationship, or has had to make an investment premised on that agreement.
- viii) For these purposes, an express stipulation for a reasonable or fair measure or price will be a sufficient criterion for the courts to act on. But even in the absence of express language, the courts are prepared to imply an obligation in terms of what is reasonable.
- ix) Such implications are reflected but not exhausted by the statutory provision for the implication of a reasonable price now to be found in section 8(2) of the Sale of Goods Act 1979 (and in the case of services, in section 15(1) of the Supply of Goods and Services Act 1982).
- x) The presence of an arbitration clause may assist the courts to hold a contract to be sufficiently certain or to be capable of being rendered so, presumably as indicating a commercial and contractual mechanism, which can be operated with the assistance of experts in the field, by which the parties, in the absence of agreement, may resolve their dispute.

4.21 *Parties manifesting an intention to displace a 'subject to contract' provision.* The Supreme Court in *RTS Flexible Systems Ltd v. Molkerei Alois Müller GmbH* (2010)⁵⁶ held that, *exceptionally*, the 'subject to contract' bar (12.04) can be disapplied if the parties have steamed ahead with performance (in that case, one party performed over two-thirds of the work), indicating a joint wish to give effect to the terms of the negotiated deal without formal signing. In this case, RTS agreed to install machinery in Müller's dairy products factory, but disputes arose over payments and liabilities during this work. RTS had received over 70 per cent of the agreed price (that price being £1.3m), but the defendant's counter-claim for allegedly defective performance was for £3m. The question was whether there was a contract and, if so, on what terms. The parties had initially contemplated (as indicated by a 'subject to contract' formula, 12.04) that they would only enter a contract by formally signing it, following satisfactory negotiations. But the Supreme Court held (1) that an implied contract had arisen, in the sense that the parties' informal agreement rested on their conduct, which manifested a joint wish to give effect to the terms of the negotiated deal without formal signing; and (2) that the parties had impliedly waived by conduct the 'subject to contract' bar (this important decision is now set out in great detail).

In March 2005, installation work had begun at an agreed price, under a letter of intent, while detailed negotiations continued. But this letter of intent expired in May. The parties contemplated a final signed agreement, the so-called proposed 'MF/1' conditions. In due course, agreed proposed written terms were established: by 26 May, the contract was substantially agreed, except for some minor points which were subject to further negotiation; by 5 July, the contract was wholly agreed, but not signed; the parties agreed variations to the arrangements in August, but again the agreement had not been signed. In short, this was

⁵⁶ [2010] UKSC 14; [2010] 1 WLR 753.

an agreement lacking only the finality of signature, and everything had occurred under the umbrella of 'subject to contract'.

The Supreme Court's decision comprises three elements.

- (1) *Intent to form a contract.* The true analysis, based on objective evaluation of this substantially fulfilled project, was that the parties intended their dealings to be governed by a contractual framework, namely, the terms of the 'MF/1' agreement. And so the first instance judge had been right to find that a contract (the so-called 'implied contract') had arisen after the lapse of the letter of intent.
- (2) *Content of the agreement.* This implied contract should be held to mirror all the points (the overall price, liquidated damages and limitation of liability clauses) contained in the proposed 'MF/1' agreement, even though the parties had initially envisaged that such an agreement would require formal signing.
- (3) *Explanation of the expiry of the 'subject to contract' phase.* There had been very substantial dealings. Indeed, over two-thirds of the projected work had been accomplished. Although those dealings had been initially 'subject to contract', a fully fledged implied contract had arisen because the parties, by their conduct, had objectively manifested an intention to waive the 'subject to contract' express formula on these facts.

Earlier in the *RTS* litigation, Christopher Clarke J, in the Technology and Construction Court, had held, as a preliminary issue, that the parties had concluded a contract, but this agreement did not incorporate the 'MF/1' terms (which included, crucially, a liquidated damages clause, capping *RTS'* liability). On appeal,⁵⁷ the Court of Appeal (Waller, Moses and Hallett LJ) reversed the finding that a contract had arisen after the lapse of the letter of intent. Therefore, the Court of Appeal held that the parties' dealings were subject to restitutionary principles only (this was, of course, reversed by the Supreme Court, which found a contract after all: see above).

Three further points arise from the *RTS* case:

- (1) *Nature of the 'implied' contract.* The Supreme Court found an implied contract on these facts. Here, the dangerous word 'implied' should be understood to refer to an agreement which was not written and which arose as an inference from the parties' conduct. It is slightly curious, but commercially sound, that this 'implied' agreement was held to mirror the express terms of the intended, but still unsigned, written agreement. Therefore, the Supreme Court gave effect to an *agreement evidenced by conduct but implicitly incorporating a complex set of express terms hammered out by the parties but never formally signed*. Only in that elaborate and qualified sense was it 'implied'.
- (2) *Implied waiver of 'subject to contract'.* Secondly, the Supreme Court's decision acknowledges that the formula 'subject to contract' can be waived, that is, overridden implicitly by the parties' dealings (or, of course, explicitly). But implicit waiver by

⁵⁷ [2009] EWCA Civ 26.

conduct will be rare. As Lord Clarke emphasised (giving the court's judgment), there must be very clear evidence of such a waiver (see paragraph 56 of his judgment, cited later in this text). The Supreme Court regarded the present facts as unusually strong, because the parties' dealings clearly indicated a shared wish not just 'to get on with the job' but to do so within a contractual framework. However, legal advisors in other cases will find it hard to predict precisely when the courts will be prepared to lift the 'subject to contract' bar, with the result that substantial requested performance becomes governed by an implied contract. On this important issue, the *RTS* case provides a two-pronged pointer: (a) the court will be ready to find an implied consensus that the 'subject to contract' regime should be lifted if there has been significant performance; provided (b) all the essential loose ends, that is, the key points of disagreement, have been settled during the negotiations, so that formalising the contract in writing, and perhaps by signature (as contemplated in the *RTS* case), has become an unnecessary ritual. Lord Clarke's approval of the *British Steel* case,⁵⁸ and his attempt to distinguish that decision (see paragraph 55 of his judgment, cited below), shows that element (a) does not suffice: no contract will be found if the matter is 'subject to contract' (or a final contract is still pending) and the parties remain in significant deadlock over a central or important prospective term (on the facts of the *British Steel* case, this deadlock concerned the extent of the supplier's liability for defective performance).

(3) *Two-sided protection achieved by finding a bilateral contract.* Thirdly, the *RTS* decision attractively gives both parties contractual causes of action: the supplier for remuneration; and the recipient of performance might make a counter-claim for allegedly defective performance, and loss flowing from that. This can be contrasted with the one-sided result in the *British Steel* case (1984),⁵⁹ where only the restitutionary award succeeded. In the *British Steel* case, the recipient could not bring a counter-claim for consequential loss because such a claim would presuppose the existence of a contract: see 2.04 and the discussion below.

Returning to the Supreme Court's decision in the *RTS* case (2010), the following passages are from Lord Clarke, who gave the court's judgment:

[47] ... [I]n a case where a contract is being negotiated 'subject to contract' and work begins before the formal contract is executed, it cannot be said that there will always or even usually be a contract on the terms that were agreed subject to contract. That would be too simplistic and dogmatic an approach. The court should not impose binding contracts on the parties which they have not reached. All will depend upon the circumstances. This can be seen from a contrast between the approach of Steyn LJ in *[Trentham (Percy) Ltd v. Archital Luxfer (1993)]*⁶⁰, which was relied upon by the judge, and that of Robert Goff J in *[British Steel]*, where Goff J held that there was no contract because there had been a failure of offer and acceptance, the parties

58 [1984] 1 All ER 504; noted S. Ball, (1983) 99 LQR 572; E. McKendrick, (1988) 8 OJLS 197, at 212, 215, 217; A. Burrows, *The Law of Restitution* (3rd edn, London, 2004), 372–81.

59 [1984] 1 All ER 504.

60 [1993] 1 Lloyd's Rep 25, CA.

having decided to postpone a binding contract until a point of negotiation had been finalised,⁶¹ 2.04] ...

[48] ... [The Court of Appeal, upholding Bingham J] in *Pagnan SpA v. Feed Products* [1987] 2 Lloyd's Rep 601 held that, although certain terms of economic significance to the parties were not agreed, neither party intended agreement of those terms to be a precondition to a concluded agreement. The parties regarded them as relatively minor details which could be sorted out without difficulty once a bargain was struck. The parties agreed to bind themselves to agreed terms, leaving certain subsidiary and legally inessential terms to be decided later.

[49] In his judgment in the Court of Appeal in the *Pagnan* case [1987] 2 Lloyd's Rep 601, 619 Lloyd LJ (with whom O'Connor and Stocker LJJs agreed) summarised the relevant principles in this way:

'(1) In order to determine whether a contract has been concluded in the course of correspondence, one must first look to the correspondence as a whole ...

(2) Even if the parties have reached agreement on all the terms of the proposed contract, nevertheless they may intend that the contract shall not become binding until some further condition has been fulfilled. That is the ordinary "subject to contract" case.

(3) Alternatively, they may intend that the contract shall not become binding until some further term or terms have been agreed ...

(4) Conversely, the parties may intend to be bound forthwith even though there are further terms still to be agreed or some further formality to be fulfilled ...

(5) If the parties fail to reach agreement on such further terms [a reference to proposition (4), just cited], the existing contract is not invalidated unless the failure to reach agreement on such further terms renders the contract as a whole unworkable or void for uncertainty.

(6) ... [I]t is for the parties to decide whether they wish to be bound and if so, by what terms, whether important or unimportant. It is the parties who are, in the memorable phrase coined by the Judge [Bingham J at first instance at page 611] "the masters of their contractual fate". Of course the more important the term is the less likely it is that the parties will have left it for future decision. But there is no legal obstacle

61 *British Steel Corporation v. Cleveland Bridge and Engineering Company* [1984] 1 All ER 504; noted S. Ball, (1983) 99 LQR 572; E. McKendrick, (1988) 8 OJLS 197, at 212, 215, 217; A. Burrows, *The Law of Restitution* (3rd edn, London, 2004), 372–81.

which stands in the way of the parties agreeing to be bound now while deferring important matters to be agreed later. It happens every day when parties enter into so-called “heads of agreement”.

...

[55] We note in passing that the *Percy Trentham* case was not a ‘subject to contract’ or ‘subject to written contract’ type of case. Nor was the *Pagnan* case, whereas part of [Goff J’s] reasoning in the *British Steel* case [in a passage quoted at paragraph 52 of the judgment in the *RTS* case] was that the negotiations were throughout conducted on the basis that, when reached, the agreement would be incorporated in a formal contract.

[56] Whether in such a case the parties agreed to enter into a binding contract, waiving reliance on the ‘subject to [written] contract’ term or understanding, will again depend upon all the circumstances of the case, although the cases show that the court will not lightly so hold.

...

[87] [The *RTS* case is] not a case like the *British Steel* case [2.04] because here all the terms which the parties treated as essential were agreed and the parties were performing the contract without a formal contract being signed or exchanged, whereas [in the *British Steel* case] the parties were still negotiating terms which they regarded as essential ... [in the *RTS* case] neither party wanted the negotiations to get in the way of the project. The project was the only important thing. The only reasonable inference to draw is that by or on 25 August, the parties had in effect agreed to waive the ‘subject to contract’ provision encapsulated [in clause 48 of the ‘MF/1’ agreement].

[88] ... The contract, once concluded on 25 August, must, as we presently see it (though the point was not fully explored before us), be treated as applicable to the whole period of contractual performance.

By contrast with the result in the *RTS* case (2010), analysed above, no contract was found in a similar case, *Whittle Movers Ltd v. Hollywood Express Ltd* (2009).⁶² Instead, the Court of Appeal in the *Whittle* case preferred to make a restitutionary award, on principles of unjust enrichment, in respect of the value of goods supplied. The *Whittle* case was decided on 11 November 2009, and it does not appear to have been cited to the Supreme Court in the *RTS* case. In the *RTS* case, argument was heard in December 2009, and judgment

⁶² *Whittle Movers Ltd v. Hollywood Express Ltd* [2009] EWCA Civ 1189; [2009] CLC 771 (Waller, Dyson and Lloyd LJ); noted by P. S. Davies, (2010) 126 LQR 175–9.

delivered in March 2010. But it will be suggested that the *Whittle* and *RTS* cases are reconcilable. This is because in the *Whittle* case the parties were still engaged in lively negotiations concerning key terms, whereas in the *RTS* case the negotiations had been completed successfully, although this fully agreed set of terms had not been formally signed off.

In the *Whittle* case, Whittle had won a tender competition for the supply of food and drinks to a chain of video stores. The parties were in negotiation for a final, written long-term supply agreement. All matters were expressly 'subject to contract' (12.04; also 1.16, 2.07, 4.21, 6.06). In the meantime, Whittle supplied goods to Hollywood, invoicing Hollywood for these supplies at the rates specified in the draft long-term supply agreement. Unfortunately, Hollywood then ceased to trade, having been bought by a third party. Hollywood purported to give six months' notice to terminate an alleged interim contract with Whittle. In response, Whittle contended (1) that there was a long-term contract, or (2) that there was no interim contract, and so it should be paid at the reasonable market rate for the goods supplied, rather than at the lower rate which would have been economically viable for Whittle only if it had secured a long-term contract. Judge Raynor QC at first instance rejected both (1) and (2), and held that Whittle was bound to accept payment under an implied interim contract and that the award should reflect the prices contemplated under the long-term contract: this involved defeat for Whittle on the question of quantum although a victory on the issue of Hollywood's liability to remunerate.

But the Court of Appeal reversed and held that Whittle was entitled to the higher level of remuneration under restitutionary principles, as mentioned at (2) above. The Court of Appeal decided that the presence of a 'subject to contract' clause prevented the finding of an implied interim contract: the court was not satisfied that the parties had agreed to waive the 'subject to agreement' bar (compare the *RTS* case, discussed above, where such an implied waiver of the 'subject to contract' clause had been found on the objective evidence of the parties' dealings). And so, under restitutionary principles, Whittle should receive a reasonable sum (awarded as a *quantum valebat*, 'for as much as the supply was worth') for the market value of its goods. The court ordered an inquiry to determine the difference between the prices already received at the depressed 'consensual' rate and the (higher) objective and market reasonable price for such goods.

In the *Whittle* case, Waller LJ said:

[15] Before it is possible to find any contract, whether 'if' or executory, it is necessary to analyse precisely the terms so as to test whether the reality is that such terms are still under negotiation and the proper answer is no contract. In R. Goff & G. H. Jones, *The Law of Restitution* (7th edition) page 662 there is a reference to an article by Professor McKendrick in which he argues that a court should not strain to find a contract because a restitutionary remedy can solve most if not all the problems (see footnote 7). That, it seems to me, is the correct approach ...

[19] ... [I]n my view not only was there no necessity to find some executory contract, there was a difficulty and thus no necessity in finding even what Goff J [in the *British Steel* case] called an 'if' contract because terms as to performance were still under negotiation [i.e. 'a contract under which if one party supplies, the other agrees to pay a reasonable remuneration']. All negotiations

were subject to contract and no binding arrangement was to come into existence until a formal document was signed.

[20] It does not follow that if goods or services were provided before the contract was signed Whittle were not entitled to some remuneration and thus the receipt of remuneration does not of itself dictate that there was a contract.

[21] Thus in my view the answer the judge should have reached was that there was no contract ...

[48] I would thus ... direct an inquiry as to whether Hollywood were unjustly enriched.

It is regrettable that the Court of Appeal's interesting decision in the *Whittle* case (2009) could not be considered in the *RTS* decision (2010), because of unfortunate timing. But, as mentioned above, they are reconcilable. The Supreme Court in the *RTS* case held that it will be unusual for facts to support a clear inference that the parties have implicitly waived a 'subject to contract' clause. Consistent with this emphasis upon the *very strongly presumptive continuing force of the 'subject to contract' bar*, the Court of Appeal in the *Whittle* case (although lacking the benefit of Lord Clarke's judgment in the *RTS* case) concluded that the parties' dealings remained under the 'subject to contract' umbrella because the parties in the *Whittle* case were still engaged in lively negotiation over significant terms within the proposed contract (but one commentator⁶³ has criticised the result in the *Whittle* case, preferring the trial judge's view that an implied contract should have been ascribed to the parties' dealings in that case). By contrast, the *RTS* case concerned performance against a background of completed negotiation on all major terms, albeit without the finality of a signed contract (as had been contemplated).

As for the award in the *Whittle* case, it is surprising that the Court of Appeal's unjust enrichment remedy, on these facts, enabled the performing party to receive an increase in remuneration, above that contemplated in their long-term contract (some goods had already been invoiced and paid for at this lower level). The decision thus remakes the nascent bargain (on the basis of which Whittle had already begun to invoice Hollywood). This award would augment the proposed 'contractual' level of payment. This is generous to the supplier and readjusts the commercial risks. Might it not have been better to have allowed the restitutionary award to reflect the actually intended level of remuneration, even though that rate was incorporated in a bargain which failed to materialise as a binding contract?

6. UPHOLDING COMPROMISE AGREEMENTS

- 4.22 Settlement or compromise agreements, whether reached in contemplation of civil proceedings or in conclusion of such litigation, are intended to bring finality to a dispute (5.20). As the Court of Appeal emphasised in *Scammell v. Dicker* (2005), considerations of general efficiency and fairness between the parties require that such an agreement should not be readily invalidated.⁶⁴ This includes difficulties in construing or applying the terms of the compromise agreement.

⁶³ P. S. Davies, (2010) 126 LQR 175–9.

⁶⁴ [2005] EWCA Civ 405; [2005] 3 All ER 838.

7. NEGOTIATION EXCLUSIVELY RESERVED TO THE PARTIES

- 4.23 As mentioned above (4.06), the parties retain a trump card, based on the principle of freedom of contract (1.08), enabling them to retain autonomy of the settlement of the terms of their proposed dealings. A case which might be rationalised in this way is *Courtney & Fairbairn Ltd v. Tolaini Bros (Hotels) Ltd* (1975), where the Court of Appeal held that no building contract arose where a landowner and developer had left open for future negotiation the fixing of 'fair and reasonable' prices for building work to be done by the developer.⁶⁵

8. THIRD PARTY RESOLUTION OF TERMS

- 4.24 The parties might agree that a blank term, normally the price, will be determined by a third party, or set of third parties. As mentioned in the context of the sale of goods (4.16), if the price is to be fixed by a panel of valuers, but one party fails to co-operate in the appointment of the valuers, section 9(2) of the Sale of Goods Act 1979 renders the party at fault liable for damages.⁶⁶ At common law, a general principle has now emerged from the House of Lords decision in *Sudbrook Trading Estate Ltd v. Eggleton* (1983) (see below), as supplemented by *Gillatt v. Sky Television Ltd* (2000)⁶⁷ (also considered below). It can be formulated as follows: the court can determine the objective content of the relevant blank term, despite the fact that the relevant third party machinery was inoperative (whether as a result of a party's default, or otherwise), provided (1) there is an objective criterion enabling the court to make this assessment, and (2) the parties have not impliedly rendered that third party resolution crucial to their prospective relations.

The *Sudbrook* case concerned leases of industrial premises, each lease containing an option permitting the tenant to purchase the reversion at a price to be agreed by valuers appointed by both parties. The lessees exercised their options to purchase, but the lessors refused to appoint a valuer. Lord Fraser said:⁶⁸

The true distinction is between those cases where the mode of ascertaining the price is an essential term of the contract, and those cases where the mode of ascertainment, though indicated in the contract, is subsidiary and non-essential ... [W]here an agreement is made to sell at a price to be fixed by a valuer who is named, or who, by reason of holding some office such as auditor of a company whose shares are to be valued, will have special knowledge relevant to the question of value, the prescribed mode may well be regarded as essential. [By contrast], where, as here, the machinery consists of valuers and an umpire, none of whom is named or identified, it is in my opinion unrealistic to regard it as an essential term. If it breaks

65 [1975] 1 WLR 297, CA.

66 The 1979 Act uses the remedy of damages; cf *Sudbrook Trading Estate v. Eggleton* [1983] 1 AC 444, HL (party frustrating an agreement that each side should appoint valuers to determine the price concerning a proposed sale of land; specific performance to compel the grant of a lease at a fair valuation).

67 [2000] 1 All ER (Comm) 461, CA.

68 [1983] 1 AC 444, 483–4, HL (a majority decision, Lord Russell of Killowen dissenting).

down there is no reason why the court should not substitute other machinery to carry out the main purpose of ascertaining the price in order that the agreement may be carried out.

In the present case the machinery provided for in the clause has broken down because the respondents have declined to appoint their valuer. In that sense the breakdown has been caused by their fault, in failing to implement an implied obligation to co-operate in making the machinery work. The case might be distinguishable in that respect from cases where the breakdown has occurred for some cause outside the control of either party, such as the death of an umpire, or his failure to complete the valuation by a stipulated date. But I do not rely on any such distinction. I prefer to rest my decision on the general principle that, where the machinery is not essential, if it breaks down for any reason the court will substitute its own machinery.

However, the fact that a third party is not named does not necessarily render the stipulation ‘inessential’ (and, conversely, the fact that he is named should not necessarily render his intervention essential – this too should be a question of construction, rather than a mechanical presumption). The true question is whether the parties have impliedly rendered the success of the stipulated third party resolution the vital hinge upon which their transaction turns. If so, the court cannot come to the rescue and itself fill the relevant blank. Thus, in *Gillatt v. Sky Television Ltd* (2000), the Court of Appeal considered a stipulation for valuation ‘of the open market value’ of shares in a private company by ‘an independent chartered accountant’.⁶⁹ The court held that this was ‘essential’ machinery which could not be bypassed by resort to the court. In this case, neither party had taken steps to appoint ‘an independent chartered accountant’, and so the relevant machinery had not ‘broken down’ for reasons outside the claimant’s control.⁷⁰ In any event, the court further held that there was no objective means of determining which manner of valuation should be adopted. Private company shares are capable of being valued on various ‘bases’: asset value, earnings, discounted cash flow, or a combination of these.

9. NO SPECIFIC PERFORMANCE OF VAGUE CLAUSES

- 4.25 *Co-operative Insurance Society Ltd v. Argyll Stores (Holdings) Ltd* (1998) (see further on this case, 18.19)⁷¹ shows that a higher degree of precision is required for specific performance or an injunction, compared with a claim for damages or debt (for an overview of these remedies, see 18.02). The approach is sound because, once specific performance is

⁶⁹ [2000] 1 All ER (Comm) 461, CA.

⁷⁰ This facet of the *Gillatt* case was applied in *Infinitel Ltd v. Artisan Contracting Ltd* [2005] EWCA Civ 758; [2006] 1 BCLC 632, at [58]; and by Aikens J in *Harper v. Interchange Group Ltd* [2007] EWHC 1834 (Comm), at [132].

⁷¹ [1998] AC 1, HL; noted by G. H. Jones, [1997] CLJ 488–91; A. M. Tettenborn, [1998] Conv 23.

ordered, the defendant is in peril of suffering quasi-criminal sanctions for contempt of court (possible fines, seizure of property or even imprisonment).⁷² It follows that the court must be able to determine clearly whether the order for specific performance has been breached; and fairness requires the defendant to receive guidance as to where the line is drawn between compliance and default.

⁷² On contempt of court, see 18.13.

III

Consideration and intent to create
legal relations

Chapter contents

1. Introduction *para. 5.01*
2. Formalities *para. 5.03*
3. Introduction to the consideration doctrine *para. 5.10*
4. Fundamental elements of consideration *para. 5.18*
5. Past consideration *para. 5.21*
6. Pre-existing statutory or other public duty *para. 5.25*
7. Pre-existing contractual duty owed to a third party *para. 5.31*
8. Consideration and the variation of contract: introduction *para. 5.33*
9. Variations to pay more than the original rate
(‘increasing pacts’) *para. 5.36*
10. Part-payment at common law (‘Decreasing pacts’, Part I) *para. 5.45*
11. The equitable doctrine of promissory estoppel
(‘Decreasing pacts’, Part II) *para. 5.54*
12. Proprietary estoppel *para. 5.64*
13. Estoppel by convention *para. 5.68*
14. Summary of types of estoppel *para. 5.72*

5

Consideration and estoppel

1. INTRODUCTION¹

5.01 Summary of main points

- (1) *Nature of 'consideration'*. Consideration to support B's promise to A can be found in any of the following four ways:
- (a) detriment suffered by A, the claimant, (unless the promised act is illegal or contrary to public policy (20.13): see points (4) ff below), or an undertaking to do something which you are already legally obliged to do (see chapter 20); or
 - (b) A, the claimant, confers a benefit on B, the defendant/promisor, or even on a third party, for example, B's child; or
 - (c) A suffers a detriment and B conversely receives a benefit (the usual case, as where A pays money to B at B's request); or
 - (d) A and B exchange lawful promises, A agreeing to do one thing and B agreeing to do another thing, as an executory bargain.

In situations (a) to (c), the benefit or detriment 'moving from A, the promisee', must be requested by B, the defendant/promisor. In situation (d), the interdependence of A and B's promises will be obvious.

- (2) *The courts do not assess the adequacy of consideration*. There is no general doctrine of a 'just price' (*iustum pretium*)² or a fair exchange. And so, bypassing the formalities of a deed, parties can convert gratuitous promises into binding agreements by resort to nominal consideration. The classic example is the grant of a lease at a so-called 'peppercorn rent'. Such use of nominal consideration creates a 'quasi-deed', a gratuitous promise specially earmarked for legal enforcement, without the bother of extensive formality. Nominal

1 On the nineteenth-century history of this topic, see M. Lobban, in W. Cornish, J. S. Anderson, R. Cocks, M. Lobban, P. Polden and K. Smith, *The Oxford History of the Laws of England*, vol. XII, 1820–1914: *Private Law* (Oxford, 2010), 358 ff.

2 Cf the French doctrine of *lésion*, on which see B. Nicholas, *French Law of Contract* (2nd edn, Oxford, 1992), 137 ff.

consideration thus signals the parties' understanding that a legally binding gratuitous promise is being created by a 'short-cut', that is, by dispensing with the formality of a deed (5.03).

- (3) *Past consideration.* Y's promise to X made in gratitude for a previous and unrequested service performed by X is regarded as gratuitous. It lacks consideration because X's prior service and Y's later promise of gratitude or acknowledgment are sequential and not linked by an initial request by Y to X. However, X can enforce Y's promise in respect of X's earlier performance if: (a) X expected to be rewarded and so was not acting gratuitously; (b) Y had requested X's performance; (c) Y later promised to reward X; and (d) the context is not one where it is against public policy to enforce the promise.
- (4) *Pre-existing statutory or public duty.* Consideration is not supplied by a person's promise or performance if the relevant act is already obligatory by virtue of a statutory or other public duty. This is because the making of that promise, or its performance, will not involve any fresh detriment.
- (5) *Pre-existing duty owed to a third party.* If A contracts with X to do something and A later contracts with Y to do the very same thing, A's promise to perform, or A's actual performance, count as consideration for Y's promise to pay A, even though A was already contractually obliged to X (in return for X's payment) to perform the very same act.
- (6) *Consideration and variation of contracts.* Consideration's operation within the field of variation of contracts has produced controversy. However, two modern Court of Appeal decisions, *Williams v. Roffey & Nicholls (Contractors)* (1991)³ and *Collier v. P & MJ Wright (Holdings) Ltd* (2007),⁴ have transformed the approach to (respectively) 'increasing pacts' and 'decreasing pacts'. The current law can be conveniently stated in two propositions:
 - (a) *Williams v. Roffey & Nicholls (Contractors)* (1991). Here, an increasing pact was *prima facie* enforceable. A's agreement to pay more for B's continuation of his unaltered contractual performance becomes enforceable on the principle that A receives B's commitment not to abandon his duties; however, B will not be able to enforce A's 'increasing pact' if the variation was procured by B's fraud or duress; (see further (7) below).
 - (b) *Collier v. P & MJ Wright (Holdings) Ltd* (2007). A decreasing pact is *prima facie* valid in equity ('promissory estoppel'), a creditor's agreement to release his debtor from the remainder of a debt, or to forgo part of a debt, becomes binding on the creditor if the debtor acts on this assurance and makes a partial payment to the creditor (if not even a part-payment is made, the position is unclear). However, the debtor will not receive the benefit of this 'decreasing pact' if he has been guilty of coercing the creditor into agreeing this favourable adjustment (see further (8) and (9) below).

³ [1991] 1 QB 1, CA.

⁴ [2007] EWCA Civ 1329; [2008] 1 WLR 643.

- (7) *Promises to pay more for the same performance.* As for (6)(a) above (increasing pacts), the courts now seem willing to circumvent the old case of *Stilk v. Myrick* (1809)⁵ and allow parties greater scope to agree binding increasing pacts even if nothing in reality is added to 'buy' the right to enhanced payment. This has been achieved by overt manipulation of the consideration rule. The turning point came in *Williams v. Roffey & Nicholls (Contractors)* (1991).⁶ Commentators accept that English law can now be stated as follows: any single 'practical benefit' will provide consideration, including a bare promise to carry on with precisely the same job. If so, consideration has been effectively eliminated from the context of increasing pacts. In short, an increasing pact is binding unless there has been fraud or duress. It might be that English law will go further and declare that consideration is no longer required in this context of increasing pacts. This was the response in the New Zealand case, *Antons Trawling Co. Ltd v. Smith* (2003)⁷ (5.31), where the apparatus of consideration was excised from this context, increasing pacts becoming enforceable, even though gratuitous, unless procured by fraud or duress.
- (8) *Gratuitous promises to reduce the level of a debt: the position at common law.* As for (6)(b) (decreasing pacts), the common law rule in *Pinnel's Case* (1602),⁸ affirmed by the House of Lords in *Foakes v. Beer* (1884),⁹ states that a promise to accept part-payment as full discharge is *prima facie* ineffective at common law. The creditor's promise to extinguish the balance of the debt is a promise to make a present of a valuable asset (the benefit of a binding debt). At common law, the creditor's promise to extinguish the balance becomes enforceable only if the agreement to accept part-payment is clothed as a deed or if 'fresh consideration' is provided, at the creditor's request, such as accelerated payment.
- (9) *Gratuitous promises to reduce the level of a debt: the position in equity.* The position just stated at (8) can change as a result of the intervention of equity. According to the Court of Appeal in *Collier v. Wright* (2007),¹⁰ the equitable doctrine of promissory estoppel can be used to render a debtor, if necessary, immune from liability to pay the balance of a debt. The unpaid part of the debt will be 'extinguished' if the creditor has received part-payment (and to this extent the debtor has relied on the creditor's promise to reduce or cancel the debt). This victory of equity over the common law rule in *Pinnel's Case* vindicates Denning J's famous *dictum* in the *High Trees* case (1947).¹¹ The law on this point is now settled by the 2007 Court of Appeal decision in the *Collier* case. Only the Supreme Court or the legislator can change the law.

5 (1809) 2 Camp 317; 6 Esp 129.

6 [1991] 1 QB 1, CA.

7 [2002] NZCA 331; [2003] 2 NZLR 23; noted by B. Coote, (2004) 120 LQR 19–23.

8 (1602) 5 Co Rep 117a (entire Court of Common Pleas).

9 (1884) 9 App Cas 605, HL.

10 [2007] EWCA Civ 1329; [2008] 1 WLR 643.

11 *Central London Property Trust Ltd v. High Trees House Ltd* [1947] 1 KB 130, 133–5.

SELECTED FURTHER READING

Critique of consideration as a requirement for the formation of agreements not under seal as deeds

P. S. Atiyah, 'Consideration: A Restatement', reprinted in P. S. Atiyah, *Essays on Contract* (Oxford, 1996)

G. H. Treitel, 'Consideration: A Critical Analysis of Professor Atiyah's Fundamental Restatement' (1976) 50 *Australian Law Journal* 439

Law Revision Committee, Sixth Interim Report on 'The Statute of Frauds and the Doctrine of Consideration' (1937, Cmd 5449), paras. 17–40 and 50; see also M. Arden, [1997] CLJ 516, 533, citing Harvey McGregor, preface to *Contract Code: Drawn up on Behalf of the English Law Commission* (Milan, 1993), 3

Increasing and decreasing pacts

G. H. Treitel, *Some Landmarks of Twentieth Century Contract Law* (Oxford, 2002), chapter 1

B. Coote, 'Consideration and Variations: A Different Solution' (2004) 120 LQR 19–23 (noting *Antons Trawling Co. Ltd v. Smith* (2003, New Zealand) (5.43))

J. O'Sullivan, 'In Defence of Foakes v. Beer' [1996] CLJ 219–28

General survey

S. Waddams, 'Principle in Contract Law: The Doctrine of Consideration', in J. W. Neyers, R. Bronaugh and S. G. A. Pitel (eds.), *Exploring Contract Law* (Oxford, 2009), 51 ff

5.02 There are three alternative reasons for enforcing a promise in English law:

- (1) formality, by use of a 'deed' (5.03 ff);
- (2) 'consideration', that is, the element of bargain (requested detriment and/or benefit, of the exchange of promises); or
- (3) induced reliance.

As regards (3), the essence is that a representee acts in response to a statement. But the representee's reliance is *not requested*, merely induced by the relevant representation. *Promissory* estoppel (see 5.72 for a summary of the types of estoppel) might give the representee the benefit of a *defence* (more time to pay, or even release from the remainder of a debt: see the discussion below). However, an active right of action in this situation of 'induced but unrequested reliance' is confined to *proprietary* estoppel in English law; in other words, only proprietary estoppel gives rise to an independent 'cause of action'. This doctrine is confined to situations where the representee has been induced detrimentally to rely in the belief that *he has, or will shortly acquire, rights in, or in respect of, the representor's land*, or the representor has unconscionably acquiesced in that misunderstanding (see the discussion below).

'Estoppel' is a general concept in private law (see also the more detailed discussion of *promissory estoppel* at 6.72).¹² In general, estoppel by representation applies if:

- (1) D makes a statement (at common law this must be a statement of past or present fact; but in equity the doctrine of 'promissory estoppel' encompasses promises);
- (2) the statement leads P to assume that X is indeed the case (or will be the case), and so P relies on that assumption;
- (3) D can be prevented by law ('estopped') from acting inconsistently with the statement; or, at least, D's legal rights might be diminished or adjusted to accommodate P's reliance.

And the general notion of estoppel is recognised in UNIDROIT's non-binding *Principles of International Commercial Contracts* (2004).¹³ Article 1.8 ('Inconsistent Behaviour') of the Principles provides:

A party cannot act inconsistently with an understanding it has caused the other party to have and upon which that other party reasonably has acted in reliance to its detriment.

The doctrine of consideration encompasses not only the *formation* of contracts (5.10 ff) but their *variation and discharge by agreement* (5.33 ff). The tradition has been to deal with both contexts in the same chapter, and this will be the approach here. Formalities, consideration, and promissory and proprietary estoppels will be discussed in that order.

2. FORMALITIES

- 5.03 In English law, the starting point is that a gratuitous promise is not enforceable. This is because the element of bargain, of 'consideration', is missing (5.10 ff). And so a promise to give money to a charity¹⁴ is not binding even if made in writing and signed. It is different if a gratuitous promise is presented as a 'deed', that is: (1) it is signed by 'the covenantor' (the promisor); (2) this signature is witnessed by a third party ('attestation'); and (3) the document is then activated by 'delivery' (this normally, but not necessarily, involves the document's physical transfer to the covenantee or his representative).¹⁵

12 Specialist works: G. Spencer Bower and A. K. Turner, *Estoppel by Representation* (4th edn, London, 2003); K. R. Handley, *Estoppel by Conduct and Election* (London, 2006); E. Cooke, *The Modern Law of Estoppel* (Oxford, 2000); and S. Wilken and T. Villiers, *The Law of Waiver, Variation and Estoppel* (2nd edn, London, 2002).

13 2nd edn, Rome, 2004; see M. J. Bonell (ed.), *The UNIDROIT Principles in Practice: Case Law and Bibliography on the UNIDROIT Principles of International Commercial Contracts* (2nd edn, Ardsley, NY, 2006), 88 ff; S. Vogenauer and J. Kleinheisterkamp (eds.), *Commentary on the UNIDROIT Principles of International Commercial Contracts* (Oxford, 2009), 186 ff.

14 Gratuitous promises to charity: *Re Hudson* (1885) 54 LJ Ch 811, Pearson J; *Re Cory* (1912) 29 TLR 18, Eve J.

15 Section 1(2)(3) of the Law of Property (Miscellaneous Provisions) Act 1989 (as amended by the Regulatory Reform (Execution of Deeds and Documents) Order 2005 (SI 2005 No. 1906, Article 7(3)); *Treitel* (12th edn, London, 2007), 3-164 ff; *Bolton Metropolitan Borough Council v. Torkington* [2004] Ch 66, CA; *Chitty on Contracts* (30th edn, London, 2008), 1-087, summarising the effect of the 2005 Order.

A deed, therefore, is exceptional because it creates a binding promise without 'consideration'. Elements (2) and (3), especially element (2), distinguish a deed from an ordinary contract in writing, even if signed (a so-called 'contract under hand').

It has just been shown that the witnessing of a covenantor's signature is a crucial and defining aspect of a valid deed. So what happens if there has been a purported witnessing ('attestation') of the covenantor's signature, but the witness did not duly attest because he was in a different room at the crucial moment of signature?

In *Shah v. Shah* (2001), the Court of Appeal held that such a purported deed (containing a promise to pay £1.5m), although technically a nullity, should be treated as binding.¹⁶ This was achieved by invoking the doctrine of estoppel by representation (see 5.72 below for a summary of the types of estoppel). The court attractively decided that the covenantor's act of handing over the deed to the other party (the 'covenantee') involved an implied 'representation', indeed an obvious suggestion, that the deed had been validly executed. The covenantee had acted sufficiently in reliance on that representation because he had lost the opportunity to demand on the spot a fresh deed to be executed, containing a true attestation.

5.04 Finally, it should be noted that, where the gift is not merely promised but actually 'executed', that is, completed, the transferee ('donee') becomes owner: as where the donor says 'I, Izaak, hereby hand you, Yehudi, as a gift this Stradivarius violin', and then hands the instrument to Yehudi. Also, an oral declaration of a trust of movable property (as distinct from land) is valid: 'I declare myself trustee of this Picasso painting for the benefit of Natasha, as sole beneficiary.'¹⁷

5.05 Most types of contract need not be made in writing (for exceptions, see the next paragraph). Sometimes, a proposed contract will require signature, not because this is a positive rule of law applicable to the transaction, but because the parties have rendered the agreement 'subject to contract' (on which generally, see 12.04). In other situations, however, parties might enter into a binding contract even though a signature has not been added to a 'signature box'. The Court of Appeal in the *Maple Leaf* case (2009) held that a company ('Lion Capital') had become party to the relevant transaction even though it (unlike the other two parties) did not sign the relevant documentation. Instead, it had notified its assent by e-mail. Longmore LJ said:¹⁸

[T]here was no requirement either within or outside the Funding Agreement that it would only become binding when signed. The most that [the party denying

16 [2001] EWCA Civ 527; [2002] QB 35, at [30] to [33]; cf *Actionstrength Ltd v. International Glass Engineering In.Gl.En SpA* [2003] 2 AC 541, HL (oral guarantee ineffective and does not give rise to an estoppel: see [8] to [9], [26] to [29], [34] to [35] and [51], explicitly distinguishing *Shah v. Shah*).

17 Express trusts concerning land must comply with the writing formality in section 53(1)(b) of the Law of Property Act 1925; a transfer ('disposition') of a 'subsisting' 'equitable interest' (whether concerning land or other property) must comply with the writing formality in section 53(1)(c); informal trusts ('resulting, implied or constructive trusts') can be created or operate under section 53(2) (see also *Yaxley v. Gotts* [2000] Ch 162, CA, examined at 5.08).

18 *Maple Leaf Macro Volatility Master Fund v. Rouvroy* [2009] EWCA Civ 1334, at [16].

contractual effect in this case] can point to is the space for the parties' signature, including that of Lion Capital, and the fact that the parties, apart from Lion Capital, did in fact sign the Funding Agreement. That does not mean that there was any consensus that the Funding Agreement was not to become binding unless it was actually signed ... It follows, in my view, that the learning in paragraphs 2-065 to 2-069 in the 30th Edition of *Chitty on Contracts* under the heading 'Prescribed Mode of Acceptance' has no relevance [in this case]. There was no prescribed mode of acceptance in this case. The fact that the agreement envisages a signature and leaves a space for those signatures is not a 'prescription' that the agreement can only become binding on the appending of signatures. The signatures are evidence and no doubt the best evidence of what had been agreed, but they are not themselves conditions of the agreement.

5.06 The main exceptional situations, where the law requires a transaction to be in writing, are: (1) certain land transactions, in accordance with the Law of Property (Miscellaneous Provisions) Act 1989 (see the next paragraph for details); (2) guarantees of debts;¹⁹ (3) cheques, bills of exchange and bills of sale;²⁰ (4) certain credit agreements;²¹ and (5) conditional fee agreements between litigants and lawyers.²² Subject to those exceptions, therefore, an agreement can take legal effect even though it was concluded orally or merely evidenced in writing. Thus, a binding agreement to 'buy' a football player for £50m, or a ship for £20m, can be made without writing, on the telephone or during a face-to-face meeting. In the 1950s, Parliament abolished the requirement, contained in the Statute of Frauds 1677,²³ that contracts for the sale of goods of even a moderate, specified value had to be evidenced in writing.

5.07 *Formalities in land transactions.* Section 2 of the Law of Property (Miscellaneous Provisions) Act 1989 provides:²⁴

(1) A contract for the sale or other disposition of an interest in land can only be made in writing and only by incorporating all the terms which the parties have expressly agreed in one document or, where contracts are exchanged, in each.

19 *Actionstrength Ltd v. International Glass Engineering In.Gl.En SpA* [2003] 2 AC 541, HL, on section 4 of the Statute of Frauds 1677; *Treitel* (12th edn, London, 2007), 5-010 ff; unwritten guarantee invalid in *Pitts v. Jones* [2007] EWCA Civ 1301; [2008] QB 706; G. Andrews and R. Millett, *The Law of Guarantees* (5th edn, London, 2008); J. O'Donovan and J. Phillips, *The Modern Contract of Guarantee* (2nd edn, London, 2010).

20 For statutory references, see *Treitel* (12th edn, London, 2007), 5-010 ff; on the Bills of Sale Act 1878 (as amended), *Online Catering Ltd v. Acton* [2010] EWCA Civ 58; [2010] 3 WLR 928 (applicable only to individuals and not to companies).

21 *Treitel* (12th edn, London, 2007), 5-010 ff.

22 Sections 58 and 58A of the Courts and Legal Services Act 1990; section 51(2) of the Senior Courts Act 1981; the Conditional Fee Agreements Order 1998 (SI 1998 No. 1860); and the Conditional Fee Agreements (Revocation) Regulations 2005 (SI 2005 No. 2305).

23 Law Reform (Enforcement of Contracts) Act 1954, following Law Revision Committee, *Sixth Interim Report on 'The Statute of Frauds and the Doctrine of Consideration'* (1937, Cmd 5449).

24 Over 200 reported cases have considered this provision: *North Eastern Properties v. Coleman* [2010] EWCA Civ 277; [2010] 3 All ER 528 is among the most recent.

(2) The terms may be incorporated in a document either by being set out in it or by reference to some other document.

(3) The document incorporating the terms or, where contracts are exchanged, one of the documents incorporating them (but not necessarily the same one) must be signed by or on behalf of each party to the contract.

(4) Where a contract for the sale or other disposition of an interest in land satisfies the conditions of this section by reason only of the rectification of one or more documents in pursuance of an order of a court, the contract shall come into being, or be deemed to have come into being, at such time as may be specified in the order.

(5) This section does not apply in relation to

- (a) a contract to grant such a lease as is mentioned in section 54(2) of the Law of Property Act 1925 (short leases);
- (b) a contract made in the course of a public auction; or
- (c) a contract regulated under the Financial Services Act 1986;

and nothing in this section affects the creation or operation of resulting, implied or constructive trusts.

5.08 The reference in section 2(5) of the Act to ‘resulting, implied or constructive trusts’ permits the courts to give effect to land transactions which fail to satisfy the formalities if the court finds some pressing ‘equitable’ factor, such as the danger that acute unfairness might otherwise result (generally on the common law and equitable distinction, see 1.25).

For example, in *Yaxley v. Gotts* (2000), B, a friend of A, orally promised A that he would be entitled to ownership of the ground floor portion of a property if he refurbished the whole property.²⁵ In fact, the property belonged to C, B’s relative. C acquiesced in A’s belief that B owned the property. The Court of Appeal held that A should be granted a ninety-nine-year lease of the ground floor because it would be ‘unconscionable’ for C to take advantage of the lack of formality in this context. This decision was an example of equitable relief, a ‘constructive trust’ awarded under section 2(5) of the 1989 Act. The purpose of this relief was to counter C’s bad faith and to prevent his unjust enrichment (the enhanced value of the property, after A’s labours).

5.09 Formality Clauses: Mediation agreements often prescribe that a binding settlement must be reduced to writing and signed by the parties or their authorised representatives. *Brown v. Rice* (2007) decides that such a formality provision governs acceptance of an

²⁵ [2000] Ch 162, CA.

offer made during a mediation meeting but expressed to be open for acceptance within a specified period after the meeting has ended.²⁶

3. INTRODUCTION TO THE CONSIDERATION DOCTRINE

- 5.10 Gratuitous promises are not enforceable unless made with the formality of a deed (an undertaking which is written, signed, witnessed and delivered,²⁷ as distinct from an ordinary signed document or a mere memorandum of agreement: 5.03.²⁸ Unless couched as a deed, a gratuitous promise is said to lack ‘consideration’. It is a *nudum pactum*, a mere moral or casual commitment, without legal effect. By contrast, a promise supported by consideration is binding, provided it is also accompanied by an ‘intent to create legal relations’ (on which see chapter 6) and there is sufficient ‘certainty’ and, furthermore, there are no problems of capacity (1.09, note 23) or illegality (chapter 20). In the nineteenth century, Sir Frederick Pollock, an influential textbook writer and long-serving editor of the *Law Quarterly Review*, defined the consideration doctrine as follows: ‘An act or forbearance of one party [the promisee], or the promise thereof, is the price for which the promise of the other [the promisor] is bought, and the promise thus given is enforceable.’²⁹ This definition was adopted in *Dunlop v. Selfridge* (1915)³⁰ by Lord Dunedin.

Lush J gave another famous definition in *Currie v. Misa* (1875) (unfortunately, this definition fails to emphasise the element of requested detriment or benefit): ‘A valuable consideration, in the sense of the law, may consist either in some right, interest, profit, or benefit accruing to the [promisor], or some forbearance, detriment, loss, or responsibility, given, suffered, or undertaken by the [promisee].’³¹

It should also be noted that the requirement of consideration operates in two contexts: formation and variation or discharge by agreement. Indeed, modern decisions have endeavoured to unpick much of its effect in the latter context (see the discussion of ‘increasing pacts’ and ‘decreasing pacts’, at 5.36 and 5.45 ff).

- 5.11 This emphasis on bargain reflects the general assumption that you get nothing (much) for free in the market-place: if you want contractual rights, you should pay for them. The upshot is that moral obligations and legal obligations do not always coincide. The courts need not apologise for drawing a line in this way; otherwise, if every promise produced legal rights, an unworkable and oppressive system of promise enforcement

26 [2007] EWHC 625 (Ch), Stuart Isaacs QC.

27 See 5.03 on the requirements for a deed.

28 An English eighteenth-century attempt to render writing a substitute for consideration was rejected in *Rann v. Hughes* (1778) 7 Term Rep 350 n.; 4 Bro PC 27 (rejecting Lord Mansfield in *Pillans v. Van Mierop* (1765) 3 Burr 1663; C. Mitchell and P. Mitchell (eds.), *Landmark Cases in the Law of Contract* (Oxford, 2008), 23 ff; S. Waddams, ‘Principle in Contract Law: The Doctrine of Consideration’, in J. W. Neyers, R. Bronaugh and S. G. A. Pitel (eds.), *Exploring Contract Law* (Oxford, 2009), 51, at 55 ff); *Anson’s Law of Contract* (29th edn, Oxford, 2010), 93.

29 *Pollock’s Principles of Contract* (13th edn, London, 1950), 133.

30 [1915] AC 847, 855 HL, *per* Lord Dunedin; privately, Pollock thought little of the consideration doctrine: see N. Duxbury, *Sir Frederick Pollock and the English Juristic Tradition* (Oxford, 2004), 204.

31 (1874–5) LR 10 Ex 153, 162.

would result. Admittedly, the doctrine of consideration – or the bargain principle – is a peculiarity of common law systems.³² A reform body recommended its removal in 1937, and the Law Commission did not include it in its abortive 1960s general contract code (21.25).³³ Neither recommendation became law, and so the doctrine of consideration survives. However, aspects of it have been modified by twentieth-century decisions. It is also interesting that it has not been incorporated into the Dubai International Financial Centre’s rules on contract law, which are otherwise based firmly on English law.³⁴

- 5.12 The fact that the common law systems are isolated in this respect from the civilian tradition prompts the question: what is the justification for the ‘consideration’ requirement? It will be suggested that consideration is a sensible and efficient mechanism to prevent bare, non-formalised gratuitous promises from being legally enforceable. The criterion of an ‘intent to create legal relations’ (see chapter 6) is insufficient. The additional requirement of ‘consideration’, the element of a bargain, both (1) is a protective rule and (2) avoids or simplifies disputes. As for (1), this doctrine shields promisors *and their estates* from ill-considered, informal and over-generous gratuitous undertakings. As for (2), the consideration doctrine avoids the need to engage in meticulous factual inquiries to determine whether a gratuitous promise was really made, or to fix its contents, or to discover whether the parties intended it to have legal force. These points will now be elaborated briefly.
- 5.13 The first function of the consideration doctrine is to protect a promisor from legal enforcement of informal gratuitous promises (even if such a promise is made in writing, it will be invalid unless made formally by deed, 5.03). Suppose X promises by telephone or letter that she will pay the appeal office of Thatcher College £1m, stipulating nothing in return. The office must wait for the deed or cheque to clear: ‘pledges’ do not count.³⁵ It is different if the money is handed over in cash, or gold bullion is delivered. These will be valid transfers, completed gifts (5.05), not requiring confirmation in writing. This protective or paternalistic policy also protects the promisor’s estate, or shareholders, or liquidators from the depletion of assets by gratuitous promises. If the father drinks or gambles away his fortune, that is one thing. But, if he enters into a series of gift promises, and then dies before satisfying them, the doctrine of consideration ensures that the folly of his promised generosity is not visited upon his offspring. Similarly, during the promisor’s lifetime, the same doctrine and the same policy ensure that his trustee in bankruptcy will have more assets to distribute to ordinary creditors who have supplied goods, etc.

32 Cf, in the USA, an informal promise to subscribe to charity is enforceable once the promisee has relied upon it: *Restatement of the Law Second, Contracts*, section 90(2).

33 E.g. the remark of Harvey McGregor QC in the preface to his *Contract Code: Drawn up on Behalf of the English Law Commission* (Milan, 1993), 3; and Law Revision Committee, *Sixth Interim Report on ‘The Statute of Frauds and the Doctrine of Consideration’* (1937, Cmd 5449).

34 Available at www.difc.ae/laws-regulations/ (Dubai International Financial Centre).

35 For gratuitous promises to charity: *Re Hudson* (1885) 54 LJ Ch 811, Pearson J; *Re Cory* (1912) 29 TLR 18, Eve J; cf, in the USA, an informal promise to subscribe to charity is enforceable once the promisee has relied upon it: *Restatement of the Law Second, Contracts*, section 90(2).

- 5.14 Secondly, the consideration doctrine efficiently filters out potential contractual disputes. Otherwise, a gratuitous promise *might* be binding and the courts would need to test each set of facts to discover whether a legally binding promise was truly intended or understood to have been intended. The additional requirement of a bargain, the element of ‘consideration’, avoids in millions of situations each year a possible dispute over whether the promise should be legally enforceable. Instead, English law provides a clear rule: a gratuitous promise is manifestly unenforceable unless formalised as a deed.
- 5.15 ‘*Marriage consideration*’. this concerns promises made in anticipation of (or at the time of) marriage, and in favour of one or both of the prospective spouses or issue of the marriage.³⁶ Equity (during the period before common law and equitable procedures and remedies were fused by the Supreme Court of Judicature Acts 1873 and 1875, 1.25) had adopted a new type of consideration, far removed from the notion of requested benefit or detriment (5.18). By this fiction, the Chancery Court had treated a property arrangement connected with a marriage as supported by ‘marriage consideration’. Consistently, equity can award specific performance in this context, the fiction ensuring that the promisee is not regarded as receiving a gratuitous promise. However, the Insolvency Act 1986 contains an anti-avoidance provision, fastening onto the reality that marriage consideration is equivalent to a gift.³⁷
- 5.16 *Liability in tort for negligent conduct*. It will be helpful here to sketch some points concerning the relationship between liability in tort for negligence and liability in contract for breach based on the claimant’s furnishing of consideration for the defendant’s express or implied promise. First, courts can recognise liability for negligent conduct even though the relevant relationship is not supported by consideration (the paradigm claim for tortious negligence is the collision between vehicles where the drivers are first brought together at the fateful moment of culpable impact). Obviously, consideration – that is, the element of a bargain – is not necessary when determining whether to recognise a duty of care in tort, including in particular the question whether to impose liability in the tort of negligence for economic loss (as distinct from physical damage to property or personal injury). In fact, many tortious duties to avoid negligence overlap with a parallel duty to exercise reasonable care based on the express or implied terms of a contract (*Henderson v. Merrett Syndicates* (1995), below).³⁸ In these ‘concurrent liability’ situations, the main practical advantage of the tort claim is a slightly more generous approach to limitation of actions (1.23). Of course, liability for negligence does not, by definition, involve strict liability. Contractual liability can *sometimes* involve this more severe form of liability (17.06). But in general the duty owed in respect of professional services is not strict (17.06). Finally, some duties of care in tort involve liability for omissions to act and not

36 *Parker and Mellows: The Modern Law of Trusts* (9th edn, London, 2008), 5-097 ff.

37 Section 339(3)(b) of the Insolvency Act 1986.

38 [1995] 2 AC 145, HL.

just for negligent performance (for both *non-feasance* and not merely for *misfeasance*: see *White v. Jones* (1995), 7.42).³⁹

Hedley Byrne & Co. v. Heller (1964)⁴⁰ began the tort of negligence's imperialistic⁴¹ expansion into the realm of liability for economic loss resulting from negligence (on its facts, liability for a negligent misstatement). In the *Hedley Byrne* case, the claimant had asked, via a third party, the defendant bankers to provide information concerning the creditworthiness of the claimant's customer. The claimant risked exposure to substantial loss (£17,000) if that customer lacked funds. The defendant bankers supplied positive information. This induced the claimant to continue to deal with this customer. But the customer defaulted. The claimant sued the bank, which had provided inaccurate information. The claim was in tort. There was no contractual relationship between these parties. The House of Lords unanimously held, establishing in the modern law a new category of negligence claim, that the defendant might have been liable in the tort of negligence for this pure economic loss (although on the facts the defendant had successfully avoided this liability by making an express disclaimer at the time the information was supplied). In this case, Lord Devlin suggested that this legal development would reduce the pressure to 'find' or 'invent' consideration in order to do justice.⁴²

5.17 Later decisions in tort make clear that liability for negligence can arise without the need to show a bargain supporting the parties' relationship. As the next case shows, the courts now use the fluid concept of an 'assumption of responsibility' (and other tests: see below) to found liability without the contractual requirement of consideration. *Customs & Excise Commissioners v. Barclays Bank plc* (2006)⁴³ contains a review of the economic loss cases in the tort of negligence. The decision shows the need to curb the expansive tendency of this tort to avoid imposing liability in a surprising and overreaching manner. That case also contains an illuminating exposition of the legal techniques, and the relevant agenda of issues, applicable when considering a 'novel' demand for the recognition of a duty of care, especially in respect of pure economic loss. As Lord Bingham said in *Customs & Excise Commissioners v. Barclays Bank plc* (2006):⁴⁴

[T]he authorities⁴⁵ disclose three tests which have been used in deciding whether a defendant sued as causing pure economic loss to a claimant owed him a duty of care in tort. The first is whether the defendant assumed responsibility for what he

39 [1995] 2 AC 207, HL.

40 [1964] AC 465, HL.

41 A. Weir, 'The Staggering March of Negligence', in P. Cane and J. Stapleton (eds.), *The Law of Obligations: Essays in Celebration of John Fleming* (Oxford, 1998), 97.

42 [1964] AC 465, 527–8, HL.

43 [2006] UKHL 28; [2007] 1 AC 181, HL.

44 *Ibid.*, at [4].

45 Citing: *Hedley Byrne & Co. Ltd v. Heller & Partners Ltd* [1964] AC 465, HL; *Ministry of Housing and Local Government v. Sharp* [1970] 2 QB 223, CA; *Smith v. Eric S Bush* [1990] 1 AC 831, HL; *Caparo Industries plc v. Dickman* [1990] 2 AC 605, HL; *Henderson v. Merrett Syndicates Ltd* [1995] 2 AC 145, HL; *White v. Jones* [1995] 2 AC 207, HL; *Spring v. Guardian Assurance plc* [1995] 2 AC 296, HL; *Williams v. Natural Life Health Foods Ltd* [1998] 1 WLR 830, HL; *Phelps v. Hillingdon London Borough Council* [2001] 2 AC 619, HL.

said and did *vis-à-vis* the claimant, or is to be treated by the law as having done so. The second is commonly known as the threefold test: whether loss to the claimant was a reasonably foreseeable consequence of what the defendant did or failed to do; whether the relationship between the parties was one of sufficient proximity; and whether in all the circumstances it is fair, just and reasonable to impose a duty of care on the defendant towards the claimant (what [an Australian judge] succinctly labelled ‘policy’). Third is the incremental test ... that: ‘the law should develop novel categories of negligence incrementally and by analogy with established categories, rather than by a massive extension of a *prima facie* duty of care restrained only by indefinable “considerations which ought to negative, or to reduce or limit the scope of the duty or the class of person to whom it is owed”’

4. FUNDAMENTAL ELEMENTS OF CONSIDERATION

5.18 An element of detriment or benefit will suffice: the claimant need not show both, although most contracts in fact involve both elements. Consideration can be furnished in one of four ways:

- (1) Detriment suffered by the claimant (unless the promised act is illegal or contrary to public policy (see chapter 20) or the undertaking to do something which you are already legally obliged to do).
- (2) The claimant confers a benefit on the defendant/promisor or even on a third party, for example on the defendant’s child.
- (3) A conjunction of benefit and detriment (the usual case). For example, in *Barry v. Davies* (2000, 3.47), the Court of Appeal held that, once a bid is made at auction, consideration is supplied by the bidder, ‘in the form of detriment to the bidder, since his bid can be accepted unless and until it is withdrawn, and benefit to the auctioneer as the bidding is driven up’.⁴⁶
- (4) There is an exchange of promises: ‘I promise to mow your lawn if you promise to feed my prize pig.’ ‘Sure, it’s a deal.’ In this situation, each promise is the price given for the other’s counter-promise; and there is no need to search for further detriment, or for immediate fulfilment of the promise.⁴⁷

In each of the situations (1) to (3), set out above, the benefit or detriment must be *requested* by the defendant/promisor. But, as Denning and Asquith LJ said in *Combe v. Combe* (1951), the request can be ‘express or implied’, that is, the fact that the claimant’s conduct was carried out or promised in exchange for the defendant’s promise can be clear from the relevant context.⁴⁸

⁴⁶ [2000] 1 WLR 1962, 1967, CA.

⁴⁷ *Treitel* (12th edn, London, 2007), 3-008; P. S. Atiyah, *Essays on Contract* (Oxford, 1986), 191; B. Nicholas, *French Law of Contract* (2nd edn, Oxford, 1992), 119–20.

⁴⁸ *Combe v. Combe* [1951] 2 KB 215, 221, 226–7, CA: on the ‘implied’ category, *Re Casey’s Patent* [1892] 1 Ch 104, CA: 5.23.

This is illustrated by *Pitts v. Jones* (2008).⁴⁹ In this case, the claimants had non-bindingly arranged to sell their shares in a company to a third party, and the defendant had agreed to sell his shares in the same company to the same third party. The defendant was keen to push through this deal. But he wrongly sensed that the claimants might pull out. And so, with misplaced anxiety, the defendant stepped in and gave the claimants oral guarantees that he would cover their losses if the third party failed to pay for the claimants' shares once they had transferred them to the third party. The claim was defeated because the oral guarantee was invalid for lack of writing (as required by section 4 of the Statute of Frauds 1677).⁵⁰ For this reason, the court's discussion of consideration, in this case, was *obiter*. On this interesting but unnecessary point, the Court of Appeal suggested that there was consideration, an element of bargain, to support the guarantee even though the claimants would have proceeded with the proposed deal without it. A party can supply 'detriment' even though he is not aware that his conduct involves any hardship and he would be prepared to act in this way without receiving a gratuitous oral guarantee. On the consideration point, Smith LJ adopted a flexible approach:⁵¹

I would hold that the claimants' co-operation was given in return for the defendant's undertaking. I would also hold that that was good *consideration notwithstanding the fact that the claimants did not consciously realise that by signing the documents they were subjecting themselves to a detriment and were giving consideration for the defendant's undertaking*. For those reasons I would hold that the defendant's undertaking was supported by consideration and was therefore a contractual agreement.

The words in emphasis are crucial: the case shows that in a commercial context the courts are prepared to apply the concept of a bargain in a flexible fashion. The court was prepared to overlook the fact of the claimants' psychological misperception: their belief that they were receiving a 'bonus' guarantee, and that they were not doing anything detrimental, that is, anything new or specific, to 'earn' it. Instead, the court gave effect to the objective presence of an element of 'detriment'. It appears that the court was willing to adopt this flexible approach because the oral assurance was (1) intended to create legal relations and (2) made in the course of a wider commercial transaction. It is difficult not to see the Court of Appeal in this case as paying anything more than lip-service to the consideration requirement. Behind the façade of technical consideration, the undisclosed and truly operative factors for the court were (1) that the oral assurance was perceived by both parties to be intended to create legal relations and (2) that the oral assurance was given as part of a wider commercial transaction.

5.19 No testing of the adequacy of consideration.⁵² Generally, the courts do not assess the adequacy of consideration, although this is tempered by specific rules governing compromises affecting non-adults or the mentally ill,⁵³ and anti-avoidance provisions in the

⁴⁹ [2007] EWCA Civ 1301; [2008] QB 706.

⁵⁰ *Actionstrength Ltd v. International Glass Engineering In.Gl.En SpA* [2003] 2 AC 541, HL, on section 4 of the Statute of Frauds 1677; *Treitel* (12th edn, London, 2007), 5-010 ff.

⁵¹ [2007] EWCA Civ 1301; [2008] QB 706, at [18].

⁵² *Anson's Law of Contract* (29th edn, Oxford, 2010), 99-100 (discussing *Haigh v. Brooks* (1839) 10 Ad & El 309; 113 ER 119, affirmed (1840) 10 Ad & El 323; 113 ER 124; and *Chappell & Co. Ltd v. Nestle* [1960] AC 87, HL).

⁵³ The court supervises the settlement of claims affecting (either on behalf of or against) children (those under 18) and mental patients: CPR 1998, Rule 21.10.

insolvency legislation.⁵⁴ Subject to those exceptions, there is no general doctrine of a 'just price' (*iustum pretium*)⁵⁵ or a fair exchange. And so, bypassing the formalities of a deed (5.03), parties can convert gratuitous promises into binding agreements through the manipulation of *nominal* consideration. The classic example, which has passed into the vernacular, is the grant of a lease at a 'peppercorn' rent. Use of nominal consideration is a 'quasi-deed': it signals the parties' understanding that a legally binding gratuitous promise is being created by a 'short-cut' route, that is, by dispensing with the formality of a deed.⁵⁶

- 5.20 *Compromises*.⁵⁷ Such arrangements deserve mention because they illustrate the pliable and pragmatic application of 'detriment' and 'benefit'. This topic also demonstrates the courts' unwillingness to use consideration as a means of ensuring an equivalent or fair exchange (see also 4.22). *Callisher v. Bischoffsheim* (1870)⁵⁸ and *Miles v. NZ Alford Estate* (1886)⁵⁹ establish that a compromise is supported by consideration provided (1) the claim is made in good faith⁶⁰ and (2) the claim has some objective plausibility (that is, it was not manifestly hopeless, vexatious or frivolous,⁶¹ or, as more recently formulated by Christopher Clarke J in *Birmingham City Council v. Forde* (2009), whether the 'doubts were fanciful or unrealistic').⁶² The 'compromise' rule applies not just to claims where formal proceedings are started but also where litigation is contemplated or a possibility. Below the surface of this analysis there are, of course, supporting factors: settlements are to be encouraged; formal proceedings should be avoided; and it would be contrary to 'finality' or 'closure' if such compromises were to be readily overturned (see also 4.22 on *Scammell v. Dicker*, 2005).⁶³

5. PAST CONSIDERATION

- 5.21 A promise made in gratitude for a previous and *unrequested* service is regarded as gratuitous and lacking in consideration. It is, therefore, unenforceable. The rationale is that the service was unrequested. Therefore, the performer, even if he was not acting benevolently but in hope of payment, took the risk of non-payment. He jumped the gun. The promise

54 Such legislation enables the courts to examine the substance and to discover whether the sale has been at a significant undervalue, for example, sections 238, 339 and 423 of the Insolvency Act 1986 (as amended), on which see *Re Kumar* [1993] 1 WLR 224, 240–1, Ferris J.

55 Cf the French doctrine of *lésion*, on which see B. Nicholas, *French Law of Contract* (2nd edn, Oxford, 1992), 137 ff; such a doctrine also applies in Jersey: *Snell v. Beadle* [2001] UKPC 5; [2001] 2 AC 304, PC.

56 Cf M. Arden, [1997] CLJ 516, 533: 'nominal consideration' is potentially the nail in the doctrine's coffin (citing Harvey McGregor QC, in the preface to his *Contract Code: Drawn up on Behalf of the English Law Commission* (Milan, 1993), 3).

57 D. Foskett, *The Law and Practice of Compromise* (7th edn, London, 2010).

58 (1870) LR 5 QB 449, CA.

59 (1886) 32 Ch D 266, 291, CA.

60 *Callisher v. Bischoffsheim* (1870) LR 5 QB 449, 452, *per* Cockburn CJ; *Cook v. Wright* (1861) 1 B & S 559.

61 *Miles v. NZ Alford Estate* (1886) 32 Ch D 266, 291, *per* Bowen LJ.

62 [2009] EWHC 12 (QB); [2010] 1 All ER 802, at [90], last two sentences.

63 [2005] EWCA Civ 405; [2005] 3 All ER 838.

to pay came too late. The element of bargain is missing. Such a promise savours of a gift. The leading decision is *Eastwood v. Kenyon* (1840).⁶⁴

In *Eastwood v. Kenyon* (1840), P had two capacities: he was executor of a will and he was guardian to T, a daughter of the relevant testator. P, as guardian, raised a loan which was devoted to educate and to promote the marriage prospects of T. T later married D. D, her husband, promised to reimburse P, the guardian (earlier, T had also promised to do so). But D refused to pay P. The court held that D had a valid defence because his promise to reimburse P was not supported by consideration. In addition, Lord Denman gave two reasons to support his decision: (1) to enforce such a promise would open the possibility of annihilating consideration as a whole; (2) it would be bad policy to encourage executors and guardians to take such lavish steps in the hope of eventual reimbursement.

The rule was applied in *Roscorla v. Thomas* (1842), where it was held that a warranty given after sale had no legal effect.⁶⁵ The rule was also applied in *Re McArdle* (1951).⁶⁶ This case concerned a mother's expenses incurred when improving a house. Her work was later acknowledged by written agreement of grown-up children. They promised her £488. The Court of Appeal held that the mother's expenses had not been requested by the children and so this promise was unenforceable.

5.22 Since 1937, it has been apparent that the past consideration rule is an unconvincing and harsh application of the bargain principle underlying the consideration doctrine. In 1937, the Law Revision Committee had recommended abolition of the 'past consideration rule', but in vain. It would be better for English law to treat such a promise as *prima facie* enforceable unless strong public policy otherwise requires.⁶⁷ No such reason can be discerned on the facts of the *Eastwood* case (5.21).

5.23 However, the suggested harshness of the 'past consideration' rule is softened by the following qualification, which was confirmed in *Pao On v. Lau Yiu Long* (1980),⁶⁸ and is traceable to *Re Casey's Patents* (1892), where Bowen LJ said:⁶⁹

Even if it were true, as some scientific students of law believe, that a past service cannot support a future promise, you must look at the document and see if the promise cannot receive a proper effect in some other way. Now, the fact of a past service raises an implication that at the time it was rendered it was to be paid for, and, if it

64 (1840) 11 Ad & El 438, Court of Queen's Bench (rejecting Lord Mansfield's moral obligation theory for grounding liability for the promise made in recognition of past services in *Hawkes v. Saunders* (1782) 1 Cowp 289, 290).

65 (1842) 3 QB 234, Court of Queen's Bench.

66 [1951] Ch 669, CA.

67 Law Revision Committee, *Sixth Interim Report on 'The Statute of Frauds and the Doctrine of Consideration'* (1937, Cmd 5449), at [32]; similarly, Denning LJ in *Ward v. Byham* [1956] 1 WLR 496, 498, CA, and *Williams v. Williams* [1957] 1 WLR 148, 151, CA, on which see 5.28 ff.

68 [1980] AC 614, 629, PC, *per* Lord Scarman.

69 [1892] 1 Ch 104, 115–16, CA.

was a service which was to be paid for, when you get in the subsequent document a promise to pay, that [subsequent] promise may be treated either as an admission which evidences or as a positive bargain which fixes the amount of that reasonable remuneration on the faith of which the service was originally rendered.

Thus, X can enforce Y's promise in respect of X's earlier performance if:

- (1) X expected to be rewarded in some way;
- (2) Y requested X's performance;
- (3) Y later promised to reward X;
- (4) if X had made an initial agreement to perform in return for reimbursement by Y, that exchange of promises would not have been contrary to public policy.

5.24 Of these, the 'request' mentioned at (2) is the key factor, and this was the element missing on the facts of *Eastwood v. Kenyon* (1840)⁷⁰ (5.21). One can rationalise the *Pao On* qualification as follows: if elements (1) and (2) are present, the parties have created an inchoate bargain. The amount of X's reward is then fixed at stage (3). Element (4) is merely a public policy safety valve (for example, if X killed T at Y's request and Y later promised to pay X for this, this 'contract killing' would not give rise to a legally enforceable right).

6. PRE-EXISTING STATUTORY OR OTHER PUBLIC DUTY

5.25 Consideration is absent if the relevant act (or promised act) is already obligatory by virtue of a statutory or other public duty. This is because satisfaction of that promise, or performance of the relevant act, will not involve any fresh detriment. Nor will the promisee receive any real legal benefit from the performance: such conduct, even if it happens to be *factually* beneficial to the promisee, was already required by statute or common law rule, so that the promisee was entitled already to be benefited by the promisor's performance (where the duty is aimed at the public at large), or at least to receive the satisfaction of seeing that such performance took place (where the performance is aimed at someone other than the promisor, as in the duty to take care of a child born to the promisee and fathered by the promisor; see the discussion of the 'child maintenance' cases at 5.28 ff).

5.26 The preceding analysis remains English law, as the House of Lords decision in *Glasbrook Bros Ltd v. Glamorgan County Council* (1925) makes clear.⁷¹

A mine-owner promised to pay local police to protect his property from trade union pickets. The police formed a garrison and were billeted at the colliery. The House of Lords held that the promise to pay the police was enforceable if the level of policing provided exceeded that required in the ordinary course of performance of the police's duty.

⁷⁰ (1840) 11 Ad & El 438, Court of Queen's Bench.

⁷¹ [1925] AC 270, 277–8, 281, HL; *Treitel* (12th edn, London, 2007), 3-046.

The Court of Appeal in the *Reading Festival* case (2006)⁷² explained the *Glasbrook* decision as follows: '[T]he police are entitled to [payment for providing] special police services if requested to do so, "special police services" being broadly defined as those over and above their general obligation to maintain law and order and keep the peace.'

The emphasis, therefore, is upon some 'special' need for extra police support.

- 5.27 The police's capacity to uphold promises to pay for 'special ... services' is now governed by section 25(1) of the Police Act 1996 (adopting without change section 15(1) of the Police Act 1964):

The chief officer of police of a police force may provide, at the request of any person, special police services at any premises or in any locality in the police area for which the force is maintained, subject to the payment to the police authority of charges on such scales as may be determined by that authority.

In *Harris v. Sheffield United FC Ltd* (1988),⁷³ the Court of Appeal held that this provision entitled the police to enforce an (express or implied) agreement for policing inside a football ground to keep belligerent fans from causing mayhem (in this case, the police made no claim for the cost of policing outside the ground).⁷⁴ However, in appropriate circumstances, as section 25(1) of the 1996 makes clear (see above), police situated outside relevant premises might be engaged in 'special ... services', if these have been requested. In the *Reading Festival* case (2006), the Court of Appeal held that police services rendered 'off-site' at a rock festival had been neither expressly nor impliedly 'requested' by the event's organisers.⁷⁵ And, in *Chief Constable of the Greater Manchester Police v. Wigan AFC* (2008),⁷⁶ the Court of Appeal held that a football club's request had been for policing within their ground at a manpower level lower than that insisted upon by the police (the police had decided that more officers were required when the club was promoted to the Premier League during the relevant two seasons). The court held (reversing Mann J at first instance): (1) that there had been no request for the services in fact provided; and (2) there had been no 'free acceptance' of those services – received during two football seasons – and so it was not possible to award an extra-contractual claim in restitution (a *quantum meruit* for the objective value of the services performed generally, 18.55). But, in his dissent, Maurice Kay LJ said:⁷⁷

Even if it had no sensible alternative, [the club] knew that, by going ahead with the matches, the chief constable would deploy his officers in accordance with the decision

72 [2006] EWCA Civ 524; [2006] 1 WLR 2005 (containing a detailed examination of the *Glasbrook* and *Harris* cases).

73 [1988] QB 77, 93, CA.

74 *Ibid.*; as explained in *West Yorkshire Police Authority v. Reading Festival Ltd* [2006] EWCA Civ 524; [2006] 1 WLR 2005, at [31].

75 *West Yorkshire Police Authority v. Reading Festival Ltd* [2006] EWCA Civ 524; [2006] 1 WLR 2005 (containing a detailed examination of the *Glasbrook* and *Harris* cases).

76 [2008] EWCA Civ 1449; [2009] 1 WLR 1580.

77 *Ibid.*, at [69].

that had been made as to what would be needed to ensure orderly behaviour of spectators. I agree with Mann J [at first instance] that, in those circumstances, it would be unjust for the club to take the benefit of the extra officers without paying for it.

5.28 *The child maintenance cases.* The general proposition that satisfaction of a public or statutory duty cannot constitute consideration (5.25 and 5.26) underpins, as we have just seen (5.27), the law concerning agreements for payment for police services. The police must do something ‘extra’ to earn the right to enforce a promise to pay for their services, and those services must have been requested by the promisor. However, in the context of child or matrimonial maintenance agreements, Denning LJ twice attacked this proposition, first in *Ward v. Byham* (1956)⁷⁸ (5.29) and then in *Williams v. Williams* (1957)⁷⁹ (5.30). In his view, which was a minority approach in these cases, the law should find consideration on such facts unless public policy specifically justifies treating the relevant agreement as invalid and hence unenforceable.

5.29 At the time of *Ward v. Byham* (1956),⁸⁰ a statutory provision⁸¹ in a 1948 Act placed the burden of maintaining illegitimate children upon the mother alone. Nowadays, the child support legislation has achieved symmetry between the sexes here by making genetic fathers liable also for the financial upkeep of children. In the *Ward* case, a father promised a mother, not his wife, to pay £1 a week if she would do two things: look after their child and make sure the child was ‘happy’. The Court of Appeal unanimously held that the father’s undertaking to pay was enforceable. The majority (Morris and Parker LJJ) applied the orthodox approach laid down in the *Glasbrook* case (1925) (5.26). In the view of Morris and Parker LJJ, the bare promise by the mother to care for the child did *not* involve consideration because it added nothing to the statutory obligation placed upon mothers under the 1948 Act. So they latched onto the fact that the second undertaking (the conferment of happiness) did supply something extra, beyond the bare statutory minimum, a supererogatory act. Morris LJ said:⁸²

[T]he father was saying, in effect: Irrespective of what may be the strict legal position, what I am asking is that you shall prove that Carol will be well looked after and happy, and also that you must agree that Carol is to be allowed to decide for herself whether or not she wishes to come and live with you. If those conditions were fulfilled the father was agreeable to pay. Upon those terms, which in fact became operative, the father agreed to pay £1 a week. In my judgment, there was ample consideration there to be found for his promise, which I think was binding.

This search for an element of requested detriment is consistent with the reasoning in the *Glasbrook* case (1925). The reasoning is logical but stretches doctrinal reason to breaking

78 [1956] 1 WLR 496, 498, CA.

79 [1957] 1 WLR 148, CA.

80 [1956] 1 WLR 496, 498, CA.

81 Section 42 of the National Assistance Act 1948.

82 [1956] 1 WLR 496, 498–9, CA; with which Parker LJ simply agreed.

point (there was, of course, scope for another approach: did the father receive a 'practical benefit' as a result of the mother's promise; see the discussion of *Williams v. Roffey Bros* at 5.40 below; he received the reassurance that the child would be cared for; and the mother's efforts would save him the practical labour of finding some other means of providing for the child, or doing so directly himself).

Denning LJ was in the minority in *Ward v. Byham*, although he reached the same decision, to uphold the father's promise. He boldly (and attractively) suggested that the law should eliminate the need to find detriment on the part of the mother. He said:⁸³

I approach the case ... on the footing that the mother, in looking after the child, is only doing what she is legally bound to do. Even so, I think that there was sufficient consideration to support the promise. I have always thought that a promise to perform an existing duty, or the performance of it, should be regarded as good consideration, because it is a benefit to the person to whom it is given. Take this very case. It is as much a benefit for the father to have the child looked after by the mother as by a neighbour. If he gets the benefit for which he stipulated, he ought to honour his promise; and he ought not to avoid it by saying that the mother was herself under a duty to maintain the child.

In Denning LJ's (minority) view, the three questions should be: (1) whether the contract was intended to create legal relations (generally on that requirement see chapter 6); (2) was the mother promising to do something beneficial to the father; and (3) was that promised act contrary to public policy? As for this last point, enforcement of promises in some contexts might clearly subvert an important public value. For example, jurors and the press should not agree that jurors will receive payment 'for carrying out their jury duties'. But Denning LJ's approach in these cases has not changed the law. He was outnumbered in both. Instead, only the House of Lords can reverse its own decisions. For the moment, therefore, the authority of the *Glasbrook* case (1925) (5.26) governs and applies not just to the context of police services but to all other statutory and public duties. Consideration will be found only if the promised performance outstrips the demands of the public duty and (it must be added) there is no public policy objection to upholding the relevant agreement.

- 5.30 Denning LJ's minority approach to this question was repeated by him in *Williams v. Williams* (1957).⁸⁴ That case was decided in a different context and concerned the objection that a promise to pay maintenance to a wife who had deserted the marriage was unsupported by consideration because she had placed herself in a situation where she had a duty – admittedly not a statutory or 'public' duty – to maintain herself. Hodson and Morris LJ, adopting orthodox reasoning, held that *prima facie* the wife was already obliged to maintain herself, having deserted her husband. But they found (by a convoluted route) consideration in the wife's undertaking, in effect, not to surrender or dispute

⁸³ [1956] 1 WLR 496, 498, CA.

⁸⁴ [1957] 1 WLR 148, CA.

her status as a wife in desertion of the husband. The minority approach, adopted by Denning LJ, dispensed with the need to find a detriment on the wife's part and focused instead on the factual benefit to the husband in being spared the inconvenience of a dispute concerning the question of maintenance. He said:⁸⁵

[A] promise to perform an existing duty is, I think, sufficient consideration to support a promise, so long as there is nothing in the transaction which is contrary to the public interest ... *By paying her 30s a week and taking this promise from her that she will maintain herself and will not pledge his credit, he has an added safeguard to protect himself from all this worry, trouble and expense. That is a benefit to him which is good consideration for his promise to pay maintenance.*

7. PRE-EXISTING CONTRACTUAL DUTY OWED TO A THIRD PARTY

5.31 This is the second aspect of the pre-existing duty doctrine (for the first, see the preceding discussion at 5.25). If A contracts with X to do something, contract 1, and A later contracts with Y to do the same thing, contract 2, and A performs, the question is whether Y can defeat A's claim by contending that there is no consideration supporting Y's promise of payment? Y's argument is that neither A's promise to perform nor A's actual performance counts as consideration because A was already contractually obliged to another to perform the very same act.

5.32 For example, suppose Blackburn, a contract law scholar, agrees with the University of Fogland for £10,000 to give a course of five lectures on the doctrine of consideration. Next he agrees with the All Profligates College (a college within the same university) to give the same lectures in the same auditorium at the same time, for £5,000. He gives the lectures, and pockets Fogland's £10,000, but the All Profligates College refuses to pay the £5,000. The College argues that Blackburn was already obliged by his contract with Fogland to do the very same thing; neither his promise to do that, nor his actual giving of the lectures, was beneficial to the College nor detrimental to him. The College, in effect, promised him a gift of £5,000. But the courts have pragmatically rejected the College's contention. Instead, it has held that consideration is supplied by Blackburn in this context.⁸⁶ In *Pao On v. Lau Yiu Long* (1980), the Privy Council affirmed that there is consideration as far as Blackburn's second *promise* (to the College) is concerned.⁸⁷ In *New Zealand Shipping Co. Ltd v AM Satterthwaite & Co. Ltd* ('*The Eurymedon*') (1975), the Privy Council affirmed⁸⁸ the same as far as *performance* of the second promise is concerned. English law is now clear, therefore, on both aspects of this conundrum (no conflict with the *Glasbrook* decision (1925)⁸⁹ (5.26) is perceived to exist, that case remaining authority only as far as pre-existing *statutory or public duties* are concerned).

⁸⁵ [1957] 1 WLR 148, 151, CA.

⁸⁶ *Treitel* (12th edn, London, 2007), 3-054, records doubts in earlier case law.

⁸⁷ [1980] AC 614, PC.

⁸⁸ [1975] AC 154, PC; similarly *Shadwell v. Shadwell* (1860) 9 CB (NS) 159.

⁸⁹ [1925] AC 270, HL.

8. CONSIDERATION AND THE VARIATION OF CONTRACT: INTRODUCTION

5.33 This is the third aspect of the pre-existing duty problem (see 5.25 and 5.31 for the first two). Here, the objection by B to A's assertion of a favourable variation *vis-à-vis* B is that A has not 'bought' that favourable variation. Once again, the logic of bargaining and of 'consideration' arises: for B can ask, 'can you, A, show, over and above the original bargain, that you have earned the right to B's favourable variation?'

5.34 In this context of consensual modification or extinction of existing contractual promises, there is a sub-division: 'increasing pacts' (a promise by B to pay for A's services or work, for example, building work) and 'decreasing pacts'⁹⁰ (B's promise to accept part-payment by A as full discharge of A's debt).

And it might be contended that there is a sub-division of each: 'interim pacts' (situations where the increasing or decreasing pact is given to a party whose obligations to work or to pay will continue to arise after the date of the relevant negotiation, as in the leading cases of *Williams v. Roffey & Nicholls* (5.40) and the *High Trees* case (5.56 to 5.58)) and 'final pacts' (situations where the pact is made after the obligation to work or to pay owed by the promisee has already arisen in full, as in *D & C Builders v. Rees* (5.51) and *Collier v. Wright* (5.59 and 5.60)).

- It now appears that both *interim and final decreasing pacts* are enforceable in equity, according to the doctrine of promissory estoppel, in that the creditor might find his right to unpaid sums extinguished by the debtor's reliance on his promise to forgo the relevant sum: *Collier v. Wright* (5.60).
- In the case of an *interim increasing pact*, the liberal resort to 'practical benefit' as sufficient consideration (see the discussion of *Williams v. Roffey & Nicholls* at 5.40) has rendered such a pact enforceable at common law.
- A *final increasing pact* (a promise to pay more for a job already completed) would appear to lack consideration, and to fall within the scope of the 'past consideration' rule (5.21).

The following discussion assumes (1) that the parties have not entered into a new agreement, having consensually terminated the old, *both parties surrendering their rights under that old contract to unperformed duties*.⁹¹ It is also assumed (2) that the parties have not varied the existing contract by *conferring mutual benefits or incurring mutual detriment*.⁹² In both cases, 'consideration' will arise from the fact that there has been an exchange of rights or exchange of releases, that is, a (two-way) bargain has been struck.

90 The upwards or downwards 'pact' terminology is adopted with gratitude from G. H. Treitel, *Some Landmarks of Twentieth Century Contract Law* (Oxford, 2002), 11.

91 *Argo Fund Ltd v. Essar Steel Ltd* [2005] EWHC 600, Aikens J; [2006] 1 All ER (Comm) 56; [2005] 2 Lloyd's Rep 203, at [51] (affirmed on other grounds at [2006] 2 All ER (Comm) 104, CA).

92 E.g. *South Caribbean Trading v. Trafigura Beheer BV* [2004] EWHC 2676 (Comm), Colman J; [2005] 1 Lloyd's Rep 128, at [105]; McKendrick, *Contract Law* (7th edn, London, 2007), 5.14, noting *Watkin & Son Inc. v. Carrig* (1941) 21 A 2d 591 (Sup Ct New Hampshire); such reasoning is regarded by Purchas LJ in *Williams v. Roffey & Nicholls* [1991] 1 QB 1, 20, CA, as 'attractive', but the court did not adopt it.

5.35 Consideration's operation within the field of variations of contracts has produced controversy. In the nineteenth century, Sir Frederick Pollock wrote on this aspect of consideration: 'the doctrine of consideration has been extended, with not very happy results, beyond its proper scope, which is to govern the formation of contracts, and has been made to regulate [also] their discharge.'⁹³ However, two modern Court of Appeal decisions, *Williams v. Roffey & Nicholls (Contractors)* (1991)⁹⁴ and *Collier v. P & MJ Wright (Holdings) Ltd* (2007),⁹⁵ have transformed the approach to both 'increasing' and 'decreasing pacts'. These respective decisions establish these propositions:

- (1) Party A's agreement to pay more (or otherwise to increase A's contribution to the contract) for B's continuation of his contractual obligations becomes enforceable on the principle that A receives B's commitment not to abandon his duties. However, B will not be able to enforce A's 'increasing pact' if the variation was procured by B's fraud or duress.
- (2) *Under principles of equity and the doctrine of promissory estoppel*, a creditor's agreement to release his debtor from the remainder of a debt, or to forgo part of a debt, becomes binding on the creditor if the debtor acts on this assurance and makes a partial payment to the creditor (if not even part-payment is made, the position is unclear; nor is the position clear if, contrary to the terms of the decreasing pact, the debtor only partially or perhaps dilatorily pays a part-payment of a part-payment, as where the part-payment is staggered in tranches, and the schedule of payments is not adhered to). However, the debtor will not receive the benefit of this 'decreasing pact' if he has been guilty of coercing the creditor into the agreement of this favourable adjustment.

The upshot of (1) and (2), therefore, is that the longhand of 'consideration' has been effectively removed from the context of post-formation agreements.

The Supreme Court has yet to ratify either proposition. Whether it should do so, and if so whether the law might be presented in a more simple and coherent fashion, are questions requiring a careful survey of the history of both topics.

9. VARIATIONS TO PAY MORE THAN THE ORIGINAL RATE ('INCREASING PACTS')

5.36 *Background.* Suppose A agrees to do work for B for £5,000. If B later agrees to pay A an extra sum for the very same job, is this 'increasing pact' a gift and so unenforceable or should the law solemnly uphold such a promise of variation? There is a conceptual point: English lawyers regard a variation of a subsisting contract as itself a species of

93 *Pollock's Principles of Contract* (13th edn, London, 1950), 150 (repeating his nineteenth-century observation); Sir Frederick Pollock was an influential textbook writer and, for many years, editor of the *Law Quarterly Review*.

94 [1991] 1 QB 1, CA.

95 [2007] EWCA Civ 1329; [2008] 1 WLR 643.

contract. Therefore, this agreed variation must be formalised by deed (5.03) or supported by fresh consideration; and, if the latter, A must promise or do something extra or different to earn the right to the promised increase.

From 1809 until 1990 (for these dates, see 5.37), the law had said that such an increasing pact is invalid because it is unsupported by consideration. Two arguments might be said to support that robust approach. First, there is the disciplinary need to hold A to the initial bargain. This is especially important if A has only won the job after a competition, formal (for example, during a competitive tender) or informal, over price. Secondly, there is the need to protect B against duress, that is, unfair pressure exerted mid-contract by A to renegotiate the terms. But there are two counter-arguments: first, freedom of contract (1.08) should permit the parties to revise the payment if circumstances change; and, secondly, the spectre of duress can and should be met by use of a special rule rather than a wholesale declaration that ‘increasing pacts’ must be invalid unless a more onerous set of obligations have been assumed by the intended payee. As for this second point, it should be noted that the English courts in the mid-1970s recognised that economic duress can invalidate the increasing pact if it results from illegitimate coercion, normally on one party to end his performance of the job forthwith, and so breach his contract. Before this development, the doctrine of duress had been confined to threats to the person or threats to damage or seize property (generally on economic duress, see 11.15).

- 5.37 *Stilk v. Myrick and its reconsideration*. Until 1991, the consideration rule in *Stilk v. Myrick* (1809)⁹⁶ had prevailed: that an ‘increasing pact’, a promise to pay more, needed to be supported by consideration. Until 1991 (see the next paragraph), this was interpreted to mean that a mere promise to carry on with one’s contractual duties would not constitute consideration.

For a fixed sum of £5 a month each, eleven sea-hands agreed to work on a sailing ship carrying a cargo between London and the Baltic and back. It was agreed that their wages would be paid on completion of the return voyage. While in Cronstadt, a port on the Baltic, two of the sailors absconded. The master of the ship agreed to pay the nine remaining loyal sailors the wages of the two deserters, if they helped to get the ship back to London. On arrival back in England, the master refused to pay the bonus. One of the loyal sailors sued for the extra sum. He failed.

- 5.38 *Discrepancies between the two reports of the Stilk v. Myrick decision*. There are two reports of the *Stilk v. Myrick* decision.⁹⁷ Espinasse’s report⁹⁸ (he was one of the counsel) says that the decision was based on public policy: the need to protect ships’ masters from coercion to pay more during the perilous stages of such voyages. A specific rule against mutiny and coercion within the merchant navy made sense. This was the very basis on

96 *Stilk v. Myrick* (1809) 2 Camp 317; 6 Esp 129; R. Halson, *Contract Law* (London, 2001), 370–85; G. H. Treitel, *Some Landmarks of Twentieth Century Contract Law* (Oxford, 2002), 11–46; G. Gilmore, *The Death of Contract* (Columbus, OH, 1974), 22–8.

97 On the discrepancy between these reports, see P. Luther, (1999) LS 526.

98 *Stilk v. Myrick* (1809) 6 Esp 129.

which Lord Kenyon had decided *Harris v. Watson* (1791).⁹⁹ Espinasse might have had many fine qualities, but his capacity as an accurate law-reporter was diminished by the fact that he was virtually deaf (and not, it seems, an accurate lip-reader).¹⁰⁰ The accuracy of his report of an *ex tempore* oral judgment (given immediately after conclusion of legal argument, without a full written text) is open to doubt.¹⁰¹

- 5.39 But what of the second report? Campbell's rival report introduces the language of consideration: because the loyal sailors had done nothing new or additionally burdensome, the master's promise was a gift. It was unsupported by consideration. According to Campbell,¹⁰² Lord Ellenborough's judgment emphasised that, before leaving London for the two-leg trip, the men had agreed impliedly 'to exert themselves to the utmost to bring the ship to her destined port'. This meant that the originally agreed rate of payment, recorded in writing,¹⁰³ covered all maritime hazards, including the extra strain created by the death or disability suffered by fellow members of the crew during the trip, or by their desertion.

Stilk v. Myrick was distinguished in later cases concerning claims for maritime wages. A mid-voyage agreement to pay an extra sum would be enforceable if, as on the extreme facts of *Hartley v. Ponsonby* (1857), a large proportion of the men had deserted or perished and the remaining crew's task had become radically different;¹⁰⁴ or if, as in *Hanson v. Royden* (1867), the bonus was in recognition of the promotion of an ordinary seaman to a higher rank, such as to petty officer or ship's surgeon. This would be a 'new job' and additional payment would be appropriate.¹⁰⁵

Campbell's report¹⁰⁶ in *Stilk v. Myrick*, based upon 'consideration', prevailed.¹⁰⁷ Indeed, this analysis became a general aspect of contract law: an 'increasing pact', a promise to pay more, needed to be supported by consideration. Until the *Roffey* case in 1991 (5.40), this was interpreted to mean that a mere promise to carry on with one's contractual duties would not provide consideration, so that the promisor could resile from his promise to pay more, without having to show that he had been the victim of fraud, exploitation or any other kind of misconduct. Indeed, the true events of the voyage in *Stilk v. Myrick* are not recorded. It is simply unknown whether the ship's hands had been guilty of any underhand dealing, duress or fraud, or whether there had been some conspiracy between the deserters and the loyal crew.

99 (1791) Peake 102.

100 Glanville Williams records an incident involving Maule J when a report of Espinasse was cited before him. Maule J claimed that he did not care for Espinasse 'or any other ass': *Glanville Williams: Learning the Law*, ed. A. T. H. Smith (12th edn, London, 2002), 44.

101 R. E. Megarry, *A Second Miscellany-at-Law* (1973), 118.

102 *Stilk v. Myrick* (1809) 2 Camp 317.

103 To satisfy a statute: 2 Geo. II, c. 36, section 1.

104 (1857) 7 E & B 872 (drastic percentage of desertion).

105 *Hanson v. Royden* (1867) LR 3 CP 47 (promotion).

106 (1809) 2 Camp 317.

107 Thus, in *Williams v. Roffey & Nichols* [1991] 1 QB 1, CA, this is the only report cited; note also Mocatta J's comments in *'The Atlantic Baron'* [1979] QB 705, 712.

5.40 ‘*Practical benefits*’: the new analysis. But the courts are now willing to circumvent the old case of *Stilk v. Myrick* (5.39) and allow parties greater scope to agree binding increasing pacts, even if nothing in reality is added to ‘buy’ the right to enhanced payment. This has been achieved by overt manipulation of the consideration rule. The turning point came in *Williams v. Roffey & Nicholls (Contractors)* (1991).¹⁰⁸

In *Williams v. Roffey & Nicholls (Contractors)* (1991), X owned a block of flats. X commissioned the defendant, the main contractor, to fit out these flats. X sub-contracted the carpentry work to the claimant, who agreed to do the work for £20,000, a low sum. But the claimant’s work was so slow that the defendant became concerned that he might become liable to pay X liquidated damages for late completion. To avoid this, the defendant tried to ‘incentivise’ the claimant by agreeing to pay him an extra sum of £575 for each completed flat. There was no suggestion that the claimant had coerced the defendant. In fact, the defendant’s incentive had a feeble effect. The claimant finished eight more flats, but then abandoned the remainder of the job. Perhaps not surprisingly, the defendant chose not to pay the claimant the £575 bonus for each of those eight flats.

At first instance, Rupert Jackson QC, sitting as an assistant recorder, held (a decision upheld on appeal) that there had been a valid renegotiation (he is quoted as follows):¹⁰⁹

In my view where the original subcontract price is too low, and the parties subsequently agree that additional moneys shall be paid to the subcontractor, this agreement is in the interests of both parties. This is what happened in the present case, and in my opinion the agreement of 9 April 1986 does not fail for lack of consideration.

This expresses an attractively common-sense and commercial perspective. Where a business party has knowingly entered into a contract for services to be performed at an uneconomic rate and, for practical reasons, that party regrets the fact that the service-provider is slow and finding the contract uneconomic, a renegotiation freely agreed to ensure timely and proper performance is ‘in everyone’s interests’. The law should not invalidate that agreement by finding that there is no consideration, no legally recognised element of bargain. The trial judge’s decision was upheld by the Court of Appeal. But this required extensive re-analysis of the requirement of consideration in this context. We will explore that reasoning below.

The Court of Appeal latched onto these facts: (1) the initial rate was uneconomic; (2) the main contractors knew they had driven a hard bargain; (3) the renegotiation was initiated by them; (4) the renegotiated rate was *prima facie* in their immediate commercial interests, because it would be more likely to spur the sub-contractors to complete their work in a timely way and to ensure the whole building project did not get bogged down; (5) there was no duress applied by the sub-contractors.¹¹⁰ On this last

108 [1991] 1 QB 1, CA; noted B. Coote, (1990) 3 *Journal of Contract Law* 23; B. Reiter, (1977) 27 *University of Toronto Law Journal* 439; M. Chen-Wishart, (1991) 14 *NZULR* 270; M. Chen-Wishart, in J. Beatson and D. Friedmann (eds.), *Good Faith and Fault in Contract Law* (Oxford, 1995), 130–2.

109 [1991] 1 QB 1, 10, CA.

110 [1991] 1 QB 1, 19–20, CA.

point, Purchas LJ said:¹¹¹ ‘The initiative in coming to the [renegotiation] agreement of 9 April came from Mr Cottrell [the defendant’s, or main contractor’s, representative] and not from the plaintiff. It would not, therefore, lie in the defendant’s mouth to assert a defence of duress.’

The Court of Appeal held that the claimant was entitled to the bonus payments,¹¹² even though the court could not discern any ‘detriment’ incurred by that party’s promise to carry on for more money (but see 5.41 at point (4) in the extract from the judgment in the *Roffey* case for the author’s suggestion that such a detriment might have existed on these facts). Instead, the court noted that consideration has two faces: detriment and benefit. Either face will do. It suffices that a benefit is conferred by the sub-contractor on the main contractor at the latter’s request. This will furnish consideration and so make the renegotiation binding.

Glidewell LJ encapsulated the law as follows:¹¹³

[T]he law on this subject can be expressed in the following proposition: (i) if A has entered into a contract with B to do work for, or to supply goods or services to, B in return for payment by B; and (ii) at some stage before A has completely performed his obligations under the contract B has reason to doubt whether A will, or will be able to, complete his side of the bargain; and (iii) B thereupon promises A an additional payment in return for A’s promise to perform his contractual obligations on time; and (iv) as a result of giving his promise, B obtains in practice a benefit or obviates a disbenefit; and (v) B’s promise is not given as a result of economic duress or fraud on the part of A; then (vi) the benefit to B is capable of being consideration for B’s promise, so that the promise will be legally binding.

This statement was adopted by Christopher Clarke J in *Birmingham City Council v. Forde* (2009).¹¹⁴

In the *Roffey* case (1991), Russell LJ added:¹¹⁵

Consideration there must still be but, in my judgment, the courts nowadays should be more ready to find its existence so as to reflect the intention of the parties to the contract where the bargaining powers are not unequal and where the finding of consideration reflect the true intention of the parties ... True it was that the plaintiff did not undertake to do any work additional to that which he had originally undertaken to do but the terms upon which he was to carry out the work were varied and, in my judgment, that variation was supported by consideration which a pragmatic approach to the true relationship between the parties readily demonstrates ... A gratuitous promise, pure and simple, remains unenforceable unless given under seal. But where, as in this case, a party undertakes to make a payment because by so doing it will gain

¹¹¹ *Ibid.*, at 21.

¹¹² Agreeing with Rupert Jackson QC, the county court trial judge.

¹¹³ [1991] 1 QB 1, 15–16, CA.

¹¹⁴ [2009] EWHC 12 (QB); [2010] 1 All ER 802, at [86].

¹¹⁵ [1991] 1 QB 1, 18–19, CA.

an advantage arising out of the continuing relationship with the promisee the new bargain will not fail for want of consideration.

After referring to *Stilk v. Myrick* (1809)¹¹⁶ and the earlier decision of *Harris v. Watson* (1791),¹¹⁷ Purchas LJ said in the *Roffey* case (1991):¹¹⁸

The two cases, *Harris v. Watson* and *Stilk v. Myrick*, involved circumstances of a very special nature, namely the extraordinary conditions existing at the turn of the 18th century under which seamen had to serve their contracts of employment on the high seas. There were strong public policy grounds at that time to protect the master and owners of a ship from being held to ransom by disaffected crews. Thus, the decision that the promise to pay extra wages even in the circumstances established in those cases was not supported by consideration is readily understandable ...

The modern cases tend to depend more upon the defence of duress in a commercial context rather than lack of consideration for the second agreement. In the present case the question of duress does not arise.

5.41 In the *Roffey* case (1991),¹¹⁹ the court identified four ‘practical benefits’:¹²⁰

(1) (a) the sub-contractor went on with the job, and so (b) the main contractor avoided the hassle of seeking substitutes (in fact this benefit was short-lived because, ultimately, the sub-contractor did cease work: but the Court of Appeal upheld the judge who had held that at that later point, work on the additional eight flats was substantially done, to justify *pro rata* payment. The job was eventually completed by substitutes);

(2) the main contractor was reassured that timely completion would avoid his having to pay liquidated damages for delay in completion of the site to X; in fact of course this reassurance was short-lived because the sub-contractor did not complete all the work, and the main contractor became liable to the site owner for late completion;

(3) the parties agreed a new and clearer system of periodical payments for the work; but the report is vague on this suggested benefit;

(4) the sub-contractor agreed to concentrate on finishing one flat at a time rather than manically trying to do every job at the same time; this would leave room for other trades to work efficiently on the site. [In fact factor (4) is two-edged: it is not

¹¹⁶ (1809) 2 Camp 317.

¹¹⁷ (1791) Peake 102.

¹¹⁸ [1991] 1 QB 1, 21, CA.

¹¹⁹ [1991] 1 QB 1, CA.

¹²⁰ E. McKendrick, *Contract Law* (7th edn, London, 2007), 5.12, creates a quintet of practical benefits, by the splitting of (1) into (a) and (b).

entirely fanciful to regard this co-operative change of performance as a possible ‘detrimment’, but this is not how the case was reasoned.]

5.42 It is obvious that the Court of Appeal in the *Roffey* case (1991)¹²¹ chose to abandon, without formally purporting to overrule, the rule in *Stilk v. Myrick* (5.37). By 1991, the old approach had ceased to be an attractive solution. It was too blunt (it was ‘over-inclusive’). At the time of *Stilk v. Myrick*, ‘duress’ was confined to threats of personal violence or physical damage to property. It was not until the 1970s that English law extended duress to encompass threats to breach a contract, that is, to inflict purely economic harm (for that development, see 11.02 ff). It is clear that this doctrinal development enabled the Court of Appeal in the *Roffey* case to bypass the blunt device of consideration and to confine a contracting party’s protection against unfairness to the specific doctrines of duress and fraud. The concept of ‘practical benefits’ was the key chosen to unlock the door to that new approach. That door had seemed to be locked by the authority of *Stilk v. Myrick*.

5.43 *Is a single practical benefit enough?* Most commentators accept that English law can now be stated as follows: any single ‘practical benefit’ will provide consideration, including factor (1) identified above, a bare promise to carry on with precisely the same job (see 5.44 for the reception of the case in later first instance decisions). If so, consideration has been effectively eliminated from the context of increasing pacts. Perhaps the Supreme Court might ratify this development. It might even go further, and declare that consideration is no longer required in this context. This has been the response in the New Zealand case, *Antons Trawling Co. Ltd v. Smith* (2003), where the New Zealand Court of Appeal said:¹²²

We are satisfied that *Stilk v. Myrick* can no longer be taken to control [cases involving increasing pacts] where there is no element of duress or other policy factor suggesting that an agreement, duly performed, should not attract the legal consequences that each party must reasonably be taken to have expected. On the contrary, a result that deprived Mr Smith of the benefit of what Antons promised he should receive would be inconsistent with the essential principle underlying the law of contract, that the law will seek to give effect to freely accepted reciprocal undertakings. The importance of consideration is as a valuable signal that the parties intend to be bound by their agreement, rather than an end in itself. Where the parties who have already made such intention clear by entering legal relations have acted upon an agreement to a variation, in the absence of policy reasons to the contrary they should be bound by their agreement.

But an increasing pact would not be binding if it resulted from (1) ‘fraud’ (no doubt including fraudulent misrepresentations, for example, false statements that the cost of

¹²¹ [1991] 1 QB 1, CA.

¹²² [2002] NZCA 331; [2003] 2 NZLR 23, at [93]; noted by B. Coote, (2004) 120 LQR 19–23; noting F. M. B. Reynolds and G. H. Treitel, ‘Consideration for the Modification of Contracts’ (1965) 7 *Malaya Law Review* 1.

performance has increased significantly) or (2) duress (11.02) or (3) perhaps (as suggested by Coote¹²³) some other forms of unacceptable underhand dealing, such as tactical under-pricing (for example, a sub-contractor deliberately under-priced the job to win the deal; this is especially reprehensible if the under-pricing occurred during a competitive tender).

- 5.44 There has been one judicial criticism of the ‘practical benefit’ reasoning. Colman J in *South Caribbean Trading v. Trafigura Beheer BV* (2004)¹²⁴ did not regard the ‘practical benefit’ reasoning in the *Roffey* case as convincing; but *Chitty on Contracts* does not accept Colman J’s challenge to this reasoning, and says that in principle a benefit can be conferred on Y by X, even though this does not involve detriment to X.¹²⁵ But Hirst J in *Anangel Atlas Compania Naviera SA v. Ishikawajima Harima Heavy Industries Co. Ltd (No. 2)* (1990)¹²⁶ applied the practical benefit analysis.

10. PART-PAYMENT AT COMMON LAW ('DECREASING PACTS', PART I)

- 5.45 *The rule in Pinnel’s Case (1602)*.¹²⁷ This rule can be formulated as follows: in the absence of a deed (5.03) or fresh consideration, part-payment does not discharge the whole debt, even though the creditor says or promises that he will forgo the unpaid part. Thus, if A owes B £1,000 and B agrees to receive £500 in complete discharge of the debt, *at common law* B remains entitled to the unpaid balance, despite this promise (for extinction of A’s right to the balance once B ‘relies’ by making part-payment, see the discussion of *Collier v. Wright* at 5.59 ff). The whole debt will be discharged by part-payment only if (1) A provides so-called ‘fresh consideration’, that is, A, at B’s request, does something extra, or A does something not strictly required (such as paying the debt earlier than the due date); or (2) B releases A from the balance by a formal deed. In (1), the law speaks of ‘fresh consideration’ (5.50).
- 5.46 The common law rule against decreasing pacts was affirmed by the House of Lords in *Foakes v. Beer* (1884),¹²⁸ applied by a majority of the Court of Appeal (Danckwerts and Winn LJ) in *D & C Builders v. Rees* (1966),¹²⁹ and followed by the Court of Appeal in *Re Selectmove* (1995),¹³⁰ admittedly without enthusiasm (see further 5.49). In this last case, the court said that the common law rule was intact and could not be subverted by resort

123 B. Coote, (2004) 120 LQR 19, 22–3.

124 [2004] EWHC 2676 (Comm); [2005] 1 Lloyd’s Rep 128, at [107].

125 *Chitty on Contracts* (30th edn, London, 2008), 3–069.

126 [1990] 2 Lloyd’s Rep 526, Hirst J; M. Chen-Wishart, *Contract Law* (Oxford, 2007), 151, and in J. Beatson and D. Friedmann (eds.), *Good Faith and Fault in Contract Law* (Oxford, 1995), 130–2.

127 *Pinnel’s Case* (1602) 5 Co Rep 117a (entire Court of Common Pleas); Law Revision Committee, *Sixth Interim Report on ‘The Statute of Frauds and the Doctrine of Consideration’* (1937, Cmd 5449), at [33].

128 (1884) 9 App Cas 605, HL; M. Lobban, in C. Mitchell and P. Mitchell (eds.), *Landmark Cases in the Law of Contract* (Oxford, 2008), 223 ff.

129 [1966] 2 QB 617, 626A, 626D, CA.

130 [1995] 1 WLR 474, CA.

to 'practical benefit' reasoning (for such reasoning, in the context of increasing pacts, see 5.41 and 5.42). However, the rule is controversial. Some support it. For example, Janet O'Sullivan in a 1996 article applauds *Foakes v. Beer*. She contends that monetary obligations should be treated as sacrosanct.¹³¹ In her opinion, once a debt, always a debt, unless the debt is reduced for good consideration supplied by the debtor. By contrast, the rule's abolition was recommended (so far in vain) by a law reform body in 1937,¹³² and Dame Mary Arden, a former Chair of the Law Commission, in an article in 1997, described this rule as 'ridiculous'.¹³³

5.47 However, there is something to be said in defence of the rule in *Pinnel's Case* (1602) and *Foakes v. Beer* (1884).¹³⁴ First, *this is a gift case*. If you owe me money, I have an asset in which I can trade. If I release you from all or part of the debt, I am making you a gift of that part from which you are released. It is axiomatic that a gratuitous promise needs to be supported by a deed. Not only must a gratuitous promise-maker be protected, by the formal requirement of a deed, from rashness, but it is arguably necessary also to protect a creditor's *inheritance and successors in title*. If enforced, the creditor's promise to accept part-payment as full discharge will reduce the value of his estate (or the creditor company's assets). The creditor might not immediately mind that. But his 'successors' will, especially his trustee in bankruptcy, or liquidator, or those financially interested after the creditor's death. Secondly, the rule in *Pinnel's Case* protects a creditor from pressure of any type and degree exerted by the debtor in attempting to procure a decreasing pact (we have seen at 5.42 how this factor has been influential in the history of the parallel doctrine concerning 'increasing pacts' and how the decision in *Williams v. Roffey & Nicholls* (1991) displaced this factor by placing confidence in the doctrine of duress to provide adequate protection). Thirdly, the rule in *Pinnel's Case* simplifies adjudication of contractual disputes: an oral promise to release or reduce a debt is not enforceable, and so disputes concerning telephone or face-to-face oral discussion are eliminated. Finally, as we shall see (5.54 ff), this common law rule has been *qualified in equity* by the doctrine of promissory estoppel, enabling the merits of the creditor and debtor's relations to be more flexibly adjusted.

5.48 *Objection to the common law rule*. It can be said, against the rule in *Pinnel's Case* (1602),¹³⁵ that the common law has ignored the creditor's 'practical benefit' in receiving part-payment now (in the hand) rather than having to chase full payment later and eventually failing, perhaps having spent money litigating. In short, the practical objection to this rule is that cash-flow realities should be taken into account. Thus, in *Foakes v.*

131 J. O'Sullivan, 'In Defence of *Foakes v. Beer*' [1996] CLJ 219–28.

132 Law Revision Committee, *Sixth Interim Report on 'The Statute of Frauds and the Doctrine of Consideration'* (1937, Cmd 5449).

133 [1997] CLJ 516, 533.

134 (1602) 5 Co Rep 117a (entire Court of Common Pleas); rule affirmed in *Foakes v. Beer* (1884) 9 App Cas 605, HL (5.26).

135 (1602) 5 Co Rep 117a (entire Court of Common Pleas).

Beer (1884), Lord Blackburn was minded to dissent on the basis that ‘a bird in the hand is worth two in the bush.’¹³⁶ But he relented and acquiesced in the other Law Lords’ decision to affirm the common law rule. However, his ‘quasi-dissent’ convinced a law reform body in 1937¹³⁷ to recommend abolition of the rule in *Pinnel’s Case*. In *Collier v. Wright (Holdings) Ltd* (2007),¹³⁸ Arden LJ quoted that 1937 report as follows:

In 1937, the Law Revision Committee ... said: ‘In *Foakes v. Beer* Lord Blackburn was evidently disposed to hold that it was still open to the House of Lords to reconsider the rule based on the *dictum*, but in deference to his colleagues who were of a different opinion he did not press his views. In a few words (at p. 622) he summed up what appears to us to be a powerful argument for the abolition of the rule. He said: ‘What principally weighs with me in thinking that Lord Coke made a mistake of fact is my conviction that all men of business, whether merchants or tradesmen, do every day recognise and act on the ground that prompt payment of a part of their demand may be more beneficial to them than it would be to insist on their rights and enforce payment of the whole. Even where the debtor is perfectly solvent, and sure to pay at last, this often is so. Where the credit of the debtor is doubtful it must be more so.’ The Law Reform Committee added: ‘In our opinion this view is as valid as it was fifty years ago, and we have no hesitation in recommending that legislation should be passed to give effect to it.’

It is instructive to compare UNIDROIT’s (non-binding) *Principles of International Commercial Contracts* (2004), Article 5.1.9 of which provides:¹³⁹ ‘(1) [A creditor] may release its right by agreement with the [debtor]. (2) An offer to release a right gratuitously shall be deemed accepted if the [debtor] does not reject the offer without delay after having become aware of it.’ In light of this clear provision it can be said that, once again, the bargain theory of contractual modification in English law can be seen to be out of step with the general juristic perception of what is commercially acceptable and reasonable.

5.49 The ‘bird in the hand’ argument resurfaced before the Court of Appeal in *Re Selectmove*,¹⁴⁰ but the court considered that it lacked the authority to subvert the rule in *Pinnel’s Case* by invoking the concept of a ‘practical benefit’ in receiving immediate partial payment. This would have been too bold a subversion of the ancient rule and only the Supreme Court can reverse its earlier decision in *Foakes v. Beer* (1884).¹⁴¹

136 (1884) 9 App Cas 605, 622, HL (at 613, 630, the Earl of Selborne LC and Lord Fitzgerald also noted that part-payment is often attractive, rather than the risk of eventual non-payment, if the debtor absconds or his assets are divided on bankruptcy in a derisory share-out).

137 Law Revision Committee, *Sixth Interim Report on ‘The Statute of Frauds and the Doctrine of Consideration’* (1937, Cmd 5449).

138 [2007] EWCA Civ 1329; [2008] 1 WLR 643, at [5].

139 2nd edn, Rome, 2004; see M. J. Bonell (ed.), *The UNIDROIT Principles in Practice: Case Law and Bibliography on the UNIDROIT Principles of International Commercial Contracts* (2nd edn, Ardsley, NY, 2006), 268–9; S. Vogenauer and J. Kleinheisterkamp (eds.), *Commentary on the UNIDROIT Principles of International Commercial Contracts* (Oxford, 2009), 571.

140 [1995] 1 WLR 474, CA; E. Peel, (1994) 110 LQR 353–6.

141 (1884) 9 App Cas 605, HL.

In *Re Selectmove* (1995), a company alleged that it had agreed with the Inland Revenue to pay its tax liability by instalments. After receipt of some of these, the Revenue applied to wind up the company as a bad debtor. The company argued, among other things, that there was a good contract that the Revenue would not foreclose for full payment so long as the instalments were paid. The Court of Appeal held, first, that no agreement had arisen because the Revenue's employee lacked authority to make any such agreement; secondly, it held that there was no consideration, applying *Foakes v. Beer*, for the agreement (nor did the doctrine of promissory estoppel apply (on which see below) not just because of the employee's lack of authority, but because the company had failed to pay the instalments on time and so had forfeited any protection in equity under that doctrine).

5.50 '*Fresh consideration*' *exonerating the debtor*. The position changes if the debtor supplies fresh consideration and so – in a sense – *purchases* the entitlement to be discharged fully. In *Pinnel's Case* (1602), Lord Coke put this colourfully, by way of example, as the debtor's gift of a horse, a hawk or a robe. Let us consider some instances of the debtor supplying consideration to support the creditor's promise to accept part-payment as full discharge.¹⁴²

- (1) *Accelerated payment in general*. Requested accelerated payment, even by one day, perhaps even less, is fresh consideration for the creditor's promise to accept half as full payment, provided the parties do a deal: 'You pay part early and I will release you from the unpaid balance.' Early payment involves detriment to the debtor and benefit to the creditor. It might be in the creditor's interest to have £500 paid on 23 March rather than the £1,000 payable on 1 April under the original agreement, if he has a 'cash-flow crisis'. It should be recalled that there is no weighing of the adequacy of consideration (for that aspect of the consideration rule, see 5.19).
- (2) *Accelerated cash payment at creditor's request*. Similarly, there might be consideration if a contract stipulates that payment should be by cheque, but the creditor later requests payment of part in cash, saying that he would then forget about the balance. It is arguable that this confers a real commercial benefit: cheques can take several days to clear and cash payment also guarantees an exchange of value, whereas cheques might be dishonoured.¹⁴³ However, the relevant change must have been requested by the creditor, rather than as a variation to suit the debtor alone.¹⁴⁴
- (3) *Part-payment by a third party in full discharge of the debt*. The creditor cannot sue the debtor for the balance if a third party, whether a friend or relative, pays part of the debt to the creditor on the footing that this will discharge the entire contract, and the creditor assents. In *Hirachand Punamchand v. Temple* (1911), a money-lender received part-payment in this way from the debtor's father.¹⁴⁵ The Court of

142 *Pinnel's Case* (1602) 5 Co Rep 117a (entire Court of Common Pleas).

143 Possibility acknowledged by Winn LJ in a *dictum* in *D & C Builders v. Rees* [1966] 2 QB 617, 633, CA.

144 *Vanbergen v. St Edmunds Properties* [1934] 2 KB 223, CA (change of place of payment not fresh consideration if variation made to suit the debtor and not the creditor).

145 [1911] 2 KB 330, CA; *Treitel* (12th edn, London, 2007), 3-108.

Appeal held that the money-lender was not entitled to claim the balance from the son. That would be a 'fraud' on the father who had stipulated that his part-payment should discharge the son's entire debt. The decision does not rest on consideration supplied by the debtor. Instead, the Court of Appeal felt determined to uphold the deal struck between the creditor and the third party, the father, the partial payor. The result seems fair and sensible. It should be noted that there is no conflict here with the rule in *Pinnel's Case* (1602) because the partial payor is a third party, the father, and not the debtor, his son. This configuration might now be rationalised as a third party benefit effective under the Contracts (Rights of Third Parties) Act 1999 (7.34), in the sense that the father and creditor agreed that the son, a third party, would be protected against a claim for the unpaid element. In the *Hirachand* case, it was clear that the payee had assented to the third party's stipulation that the part-payment would preclude any further recourse by the payee against the debtor. But in other cases this assent has been the subject of dispute, because this context often produces factual confusion whether the intended payee's keeping of, or his act of cashing, a cheque given in full and final settlement discloses an accord and satisfaction. In *IRC v. Fry* (2001),¹⁴⁶ Jacob J reviewed the authorities on that question, which is one of offer and acceptance, noting the leading discussion by Lloyd LJ in *Stour Valley Builders v. Stuart* (1992).¹⁴⁷

- (4) *Debt is disputed in good faith.* The rule in *Pinnel's Case* (1602)¹⁴⁸ applies where the debt itself is an ascertained, or ascertainable, sum and it is manifestly enforceable in law for this amount. By contrast, if the debt's existence or validity, or its amount, were genuinely disputed on objectively reasonable grounds, part-payment 'in full and final settlement' would constitute a final discharge, in accordance with the compromise or settlement rule (5.20).¹⁴⁹

5.51 Absence of fresh consideration: part-payment by cheque. In *D & C Builders v. Rees* (1966), a builder received a cheque from Mrs Rees for part of his genuine claim.¹⁵⁰ The majority judges, Danckwerts and Winn LJ, held that the payor, Mrs Rees, still owed the balance: payment by cheque, rather than cash, did not constitute fresh consideration.

In D & C Builders v. Rees (1966), Mrs Rees, the debtor, unsuccessfully contended that the creditor had received fresh consideration because payment by cheque relieved him of the burden and hazard of carrying lots of coins or notes by giving him a cheque instead. Certainly,

¹⁴⁶ [2001] STC 1715; [2002] BTC 3.

¹⁴⁷ Court of Appeal, 21 December 1992, Lloyd LJ and Connell J, reported [2003] TCLR 8; *The Times*, 22 February 1993; this is a learned judgment, demonstrating that *Day v. McLea* (1889) 22 QB 610, CA, has survived and that it supports the statement summarised in the *Stour Valley* case, despite American textbook suggestion to the contrary.

¹⁴⁸ (1602) 5 Co Rep 117a (entire Court of Common Pleas); rule affirmed in *Foakes v. Beer* (1884) 9 App Cas 605, HL (5.46).

¹⁴⁹ *Ferguson v. Davies* [1997] 1 All ER 315, CA (*dicta*: because debtor had admitted he was fully liable); *Wigan v. Edwards* (1973) 1 ALR 497 (High Court of Australia).

¹⁵⁰ [1966] 2 QB 617, CA, overruling *Goddard v. O'Brien* (1882) 9 QBD 37, Divisional Court.

it is unsafe to carry money in most parts of the Kingdom, for which reason Her Majesty the Queen, and her predecessors, do not carry cash. But the Court of Appeal rightly held that part-payment by cheque is really the equivalent of part-payment in cash. In making out a cheque rather than paying in cash, the debtor is not doing anything which is financially more onerous. Therefore, part-payment by cheque is not an exception to the rule in *Pinnel's Case* (1602).¹⁵¹ The balance remains due.

Lord Denning MR found his way to the same result by a quite different route (adopting his preferred promissory estoppel analysis, but declaring Mrs Rees to lack 'clean hands'). His approach was for some time considered to be a minority judgment, but the Court of Appeal in *Collier v. Wright (Holdings) Ltd* (2007)¹⁵² (5.59 ff) thought that he had been sufficiently supported by Danckwerts LJ.¹⁵³ Lord Denning MR in the *D & C Builders* case considered that *prima facie* the balance had been extinguished in equity (promissory estoppel) by the creditor's promise to accept part-payment as full discharge. But Lord Denning held that the balance, after all, was still owed on these facts because Mrs Rees lacked 'clean hands' and so could not successfully invoke fastidious equity's assistance. She lacked 'clean hands' because, in Lord Denning's view, she had exploited the builder's cash-flow crisis: indeed, she had coerced him into accepting merely part-payment.

5.52 *No fresh consideration if joint debtor only pays his arithmetical share.* A joint debtor is liable directly to the creditor to pay the whole of the debt (but the individual debtor who paid can later claim a contribution from the other joint debtors if he pays more than his share). The Court of Appeal in *Collier v. Wright (Holdings) Ltd* (2007)¹⁵⁴ (5.59 ff) held that a promise by a creditor to accept payment from a joint debtor of a share of the total debt is subject to the rule in *Pinnel's Case* (1602).¹⁵⁵ And so, although the creditor had agreed to accept this part-payment and to pursue the other joint debtors for the balance, the joint debtor who had paid only in part (as now agreed) nevertheless remained liable to pay the rest. There was no consideration for any release of that joint debtor from the balance of the debt.

5.53 *Other concessions or variations at common law: 'waiver' and 'forbearance'.* So far we have been considering promises to accept part-payment as full discharge of the debt. But other types of concessionary pacts might favour a debtor. The creditor might promise:

- (1) to give the debtor more time to pay; or

151 (1602) 5 Co Rep 117a (entire Court of Common Pleas); rule affirmed in *Foakes v. Beer* (1884) 9 App Cas 605, HL (5.46).

152 [2007] EWCA Civ 1329; [2008] 1 WLR 643.

153 Danckwerts LJ's judgment in the *D & C Builders* case, [1966] 2 QB 617, 625–7, is short: see 5.60 for comment.

154 [2007] EWCA Civ 1329; [2008] 1 WLR 643, at [5].

155 (1602) 5 Co Rep 117a (entire Court of Common Pleas); rule affirmed in *Foakes v. Beer* (1884) 9 App Cas 605, HL (5.46).

- (2) to accept one currency rather than the contractual currency, for example, US dollars rather than Japanese yen, or UK sterling instead of Kenyan shillings (*Alan v. El Nasr* (1972),¹⁵⁶ noted later in this paragraph); or
- (3) to change the place of payment, for example, London rather than Hong Kong.¹⁵⁷ The common law doctrine of 'waiver' (sometimes known as 'forbearance') can give effect to such a concession.

An illustration of waiver of a non-monetary obligation is *Charles Rickards Ltd v. Oppenheim* (1951).¹⁵⁸

In *Charles Rickards Ltd v. Oppenheim* (1951), the defendant commissioned the claimants to add the body to a Rolls-Royce chassis. But the claimant was absurdly slow in doing the job, and so the defendant despaired and withdrew the order. This was a case of three missed chances to perform on time: (1) the defendant customer had already waived the date for completing this task, whereupon (2) the plaintiff had further delayed; (3) then the defendant gave the claimant an extension and a clear ultimatum, but the claimant again missed the deadline.

The Court of Appeal held that at stage (3) the period given was reasonable in length and that, once the claimant had failed to meet this second deadline, the defendant customer had been entitled to terminate the contract and demand repossession of its chassis. This case shows that waiver of a contractual deadline does not prevent the party who has made this concession from setting a new deadline to which the other party must strictly adhere.

As for the basic operation of waiver in this context, Denning LJ explained:¹⁵⁹

If the defendant, as he did, led the plaintiffs to believe that he would not insist on the stipulation as to time, and that, if they carried out the work, he would accept it, and they did it, he could not afterwards set up the stipulation as to the time against them. Whether it be called waiver or forbearance on his part, or an agreed variation or substituted performance, does not matter. It is a kind of estoppel. By his conduct he evinced an intention to affect their legal relations. He made, in effect, a promise not to insist on his strict legal rights. That promise was intended to be acted on, and was in fact acted on. He cannot afterwards go back on it.

The three strands of waiver, estoppel (see 5.72 for a summary of the types of estoppel) and 'binding variations' (contractual changes supported by requested consideration) often become intertwined.¹⁶⁰ *Alan v. El Nasr* (1972) further illustrates this doctrinal intersection.¹⁶¹

¹⁵⁶ [1972] 2 QB 189, CA: on this case, see A. Burrows, *A Casebook on Contract* (2nd edn, Oxford, 2009), 143–5.

¹⁵⁷ *Vanbergen v. St Edmunds Properties* [1934] 2 KB 223, CA (change of place of payment not fresh consideration if change made to suit the debtor and not the creditor).

¹⁵⁸ [1950] 1 KB 616, CA.

¹⁵⁹ *Ibid.*, at 623.

¹⁶⁰ A. Phipps, 'Resurrecting the Doctrine of Common Law Forbearance' (2007) 123 LQR 286–313.

¹⁶¹ [1972] 2 QB 189, CA: on this case, see A. Burrows, *A Casebook on Contract* (2nd edn, Oxford, 2009), 143–5.

In *Alan v. El Nasr* (1972), the contract concerned three successive shipments of coffee, for which the price was in Kenyan shillings, payable in three instalments. However, the seller accepted payment in English pounds in respect of the first two shipments. This was a variation of the contract's original terms. The parties found themselves in dispute concerning the appropriate currency for the third payment, because at that point the English pound had been devalued. The Court of Appeal held that the creditor was bound to be consistent. He must accept payment in English pounds for the third payment. This reflected the parties' dealings. 'Waiver' had occurred. The originally stipulated currency of payment could no longer be insisted upon. The various tributaries of 'fair dealing' are explored in the three judgments: (1) Lord Denning MR argued that the basis for this might be a general principle of fair dealing, involving a fusion of 'common law waiver' and 'equitable estoppel';¹⁶² (2) Megaw LJ reached the same result by simply applying the notion of 'waiver'; and (3) Stephenson LJ found that a fresh set of terms had arisen: a binding variation.

Despite Lord Denning's attractive suggestion in *Alan v. El Nasr*, the doctrine of 'common law waiver' continues to be described in the books as distinct from promissory estoppel (on which see the next paragraph). Historically, this is true. But functionally they appear to operate quite similarly and, as *Alan v. El Nasr* shows, even identically in some contexts.

11. THE EQUITABLE DOCTRINE OF PROMISSORY ESTOPPEL (‘DECREASING PACTS’, PART II)¹⁶³

5.54 *Main factors.* This form of estoppel consists of the following elements (see 5.72 for a summary of the types of estoppel):

- (1) There must be a clear and unambiguous representation, by words or conduct, regarding the past, present *or future*.
- (2) The representee *relies* on this (some form of reliance is necessary, but the court can decide that there is *insufficient* reliance to justify estoppel).¹⁶⁴
- (3) Thereafter, the representor can validly give reasonable notice of his wish to reassert his strict legal rights.¹⁶⁵

¹⁶² *Charles Rickards Ltd v. Oppenheim* [1950] 1 KB 616, 623, CA (5.53).

¹⁶³ Specialist works: G. Spencer Bower and A. K. Turner, *Estoppel by Representation* (4th edn, London, 2003); K. R. Handley, *Estoppel by Conduct and Election* (London, 2006), chapter 13; E. Cooke, *The Modern Law of Estoppel* (Oxford, 2000); S. Wilken and T. Villiers, *The Law of Waiver, Variation and Estoppel* (2nd edn, London, 2002); M. Chen-Wishart, 'A Bird in the Hand: Consideration and Promissory Estoppel', in A. Burrows and E. Peel (eds.), *Contract Formation and Parties* (Oxford, 2010); B. McFarlane, 'Contract Formation: Promissory Estoppel', in A. Burrows and E. Peel (eds.), *Contract Formation and Parties* (Oxford, 2010).

¹⁶⁴ *'The Post Chaser'* [1982] 1 All ER 19, 25B–27, Goff J (representee's reliance insufficient).

¹⁶⁵ *Tool Manufacturing Co. Ltd v. Tungsten Electric Co. Ltd* [1955] 1 WLR 761, HL.

- (4) Subject to this last point, the representor is estopped (that is, prevented by law) from acting inconsistently with his representation.
- (5) The representee's protection will be adjusted to the extent that justice demands.
- (6) But promissory estoppel (being rooted in broad notions of equity) will not protect a representee if he comes 'with unclean hands' (for example, because he has coerced or cheated the representor into making the statement).¹⁶⁶

5.55 *The leading nineteenth-century decision.* In *Hughes v. Metropolitan Railway* (1877), the House of Lords embraced the doctrine of promissory estoppel, although this decision was not concerned with the variation of a debt.¹⁶⁷

The facts were as follows. A covenant in his lease obliged the tenant of a property to repair the property on the giving of six months' notice by the landlord. After such a notice had been served by the landlord, the parties negotiated unsuccessfully for the purchase by the tenant of the freehold. The tenant plausibly contended that during these negotiations the landlord had implicitly indicated that the tenant would have more time to repair. When these negotiations petered out, the landlord attempted to forfeit the lease, relying on the lapse of six months from the date of the repair notice. The House of Lords held that the landlord was estopped from acting in this inconsistent, unfair and even oppressive fashion. It was only fair and reasonable that the tenant should be given more time to comply with that obligation. There was no question of extinguishing the duty to repair, merely the granting of a stay on the landlord's self-help right to obtain forfeiture of the lease. Lord Cairns LC formulated the following general principle governing this species of estoppel:¹⁶⁸

But it is the first principle upon which all Courts of Equity proceed that if parties who have entered into definite and distinct terms involving certain legal rights – certain penalties or legal forfeiture – afterwards by their own act or with their own consent enter upon a course of negotiation which has the effect of leading one of the parties to suppose that the strict rights arising under the contract will not be enforced, or will be kept in suspense, or held in abeyance, the person who otherwise might have enforced those rights will not be allowed to enforce them where it would be inequitable having regard to the dealings which have thus taken place between the parties.

5.56 *The suspension/extinction debate.* The doctrine of promissory estoppel shot to greater prominence following a bold *dictum* of Denning J in the *High Trees* case (1947).¹⁶⁹

The case concerned a block of flats, High Trees House, in London. The landlord was the parent company. The head tenant held a lease for ninety-nine years. This tenant was the landlord's subsidiary company. The rent was £2,500 a year. The head tenant sub-let flats in the block

166 *D & C Builders v. Rees* [1966] 2 QB 617, CA (Lord Denning MR withholding estoppel's protection because Mrs Rees (the debtor) had unfairly coerced the builder (the creditor) into accepting part-payment).

167 (1877) 2 App Cas 439, HL.

168 *Ibid.*, at 448, HL; *Birmingham & District Land Co. v. London & NW Railway Co.* (1888) 40 Ch 268, CA.

169 *Central London Property Trust Ltd v. High Trees House Ltd* [1947] 1 KB 130, 133–5; Denning later wrote about his theory in 'Recent Developments in the Doctrine of Consideration' (1952) 15 MLR 1.

to sub-tenants. In 1940, enemy bombs began to fall on London. Even before the bombing started, Londoners had been leaving in droves to seek shelter in the less vulnerable counties surrounding London. Such fugitives from the blitz included many of the sub-tenants of High Trees House. As a result, the head tenant was now in financial difficulty. And so the landlord made a concession: to receive half the rent, £1,250, as long as these wartime difficulties prevailed. This rent reduction operated from 1939 to 1945. In the later stages of the war, the threat of air raids had diminished markedly, although 'V1' flying bombs and 'V2' rockets were still a hazard. Sub-tenants had gradually resumed occupation of the flats. However, in 1941, the landlord had gone into liquidation. In 1945, the receiver woke up to the fact that the true rent was £2,500, and he asked the head tenant for the arrears, as well as for a future rent at £2,500. In the present action, the receiver was seeking a declaration from the court that he could reassert the £2,500 figure for the last two quarters of 1945, and thereafter. Denning J granted the declaration sought. This was the case's *ratio*.

5.57 But Denning J, in further remarks unnecessary for the decision, and therefore strictly *obiter dicta*, asserted that equity's doctrine of promissory estoppel was not confined to giving debtors more time (as noted at 5.55 above, the tenant in the *Hughes* case was given more time to make repairs). In the view of Denning J, promissory estoppel might operate to ensure that a creditor honoured his promise to forgo part of a debt, even though that promise to forgive the debtor the relevant sum was unsupported by fresh consideration. In short, Denning J's suggestion was that estoppel could 'extinguish' and not merely 'suspend' a debt. If so, equity's doctrine of promissory estoppel would contradict the common law rule in *Pinnel's Case*,¹⁷⁰ which preserves the creditor's strict right to payment at common law (in the absence of a deed or fresh consideration, 5.45). Denning J felt bound to turn to equity's promissory estoppel because common law estoppel by representation was not flexible enough. This is because *Jorden v. Money* (1854) is regarded as House of Lords authority that common law estoppel requires a representation of a past or present fact and does not extend to promises of future conduct or future abstention.¹⁷¹

5.58 The decision (the *ratio*) in the *High Trees* case was unremarkable (5.56). But the *dictum* (as Denning J well knew) was a 'bombshell' in the law. The latter aspect of the case provoked a major question: (1) Was Denning J correct to suggest in his *dictum* that equity, outflanking the common law rule in *Pinnel's Case*, can legitimately treat a debt (or part of it) as 'extinguished' by the creditor's promise to reduce or release the sum owed? (2) If so, what type of 'reliance' is necessary before the debtor could receive this superior and permanent form of protection? The Court of Appeal in *Collier v. P & MJ Wright (Holdings) Ltd* (2007)¹⁷² (5.59 ff) answered 'yes' to question (1). As for question (2), the court adopted Lord Denning's view that 'reliance need only be the debtor's part-payment' (before this, a different form of reliance had seemed to be required, Lord Hodson in *Ajayi v. Briscoe*

170 (1602) 5 Co Rep 117a (entire Court of Common Pleas).

171 (1854) 5 HL Cas 185.

172 [2007] EWCA Civ 1329; [2008] 1 WLR 643 (noted by A. Trukhtanov, (2008) 124 LQR 364–8).

(1964)¹⁷³ having suggested that ‘the promise only becomes final and irrevocable if the promisee cannot resume his position’). If the *Collier* decision (2007) prevails – and only the Supreme Court can disturb it – this case will have removed sixty years of doctrinal uncertainty, especially concerning question (1) above. Therefore, the *Collier* decision requires scrutiny.

5.59 The *Collier* case (2007)¹⁷⁴ concerned these facts.

Collier was one of three partners liable jointly and severally to Wrights. This meant that each partner could be sued for the full amount of the debt. Collier alleged that he and the Wrights had reached an agreement that, if he paid one-third of the total debt (that is, his notional per capita share), he would be released from his joint liability for the balance. Collier paid this one-third share. But, after the other two partners became bankrupt, the Wrights sued him for the unpaid two-thirds. The question of Collier’s liability arose in insolvency proceedings. Collier was attempting to set aside a ‘statutory demand’ (a preliminary requirement to making a person bankrupt) made by the Wrights against him. To do so, he needed to show a real prospect of success on the merits at trial. On that question, the Court of Appeal first applied *Pinnel’s Case*¹⁷⁵ and held that Collier was still liable at common law as a joint debtor for the balance. However, the Court of Appeal held that Collier should be allowed at a final hearing (the case had come before the Court of Appeal as a preliminary question to test the legal merits of Collier’s attempted defence) to contend that the doctrine of promissory estoppel might protect him against liability to pay more than his agreed one-third share.

5.60 In the *Collier* case (2007), Arden LJ, with the support of her fellow judges, held¹⁷⁶ that the *D & C Builders* case (1966)¹⁷⁷ is binding Court of Appeal authority for these propositions:

[T]hat, if (1) a debtor offers to pay part only of the amount he owes; (2) the creditor voluntarily accepts that offer, and (3) in reliance on the creditor’s acceptance the debtor pays that part of the amount he owes in full, the creditor will, by virtue of the doctrine of promissory estoppel, be bound to accept that sum in full and final satisfaction of the whole debt. For him to resile will of itself be inequitable. In addition, in these circumstances, the promissory estoppel has the effect of extinguishing the creditor’s right to the balance of the debt. This part of our law originated in the brilliant *obiter dictum* of Denning J, as he then was, in the *High Trees* case. To a significant degree it achieves in practical terms the recommendation of the Law Revision Committee chaired by Lord Wright MR in 1937.¹⁷⁸

173 [1964] 1 WLR 1326, PC; a view favoured by *Treitel* (12th edn, London, 2007), 3–116 (at least prior to the decision in *Collier v. Wright* (2007)).

174 [2007] EWCA Civ 1329; [2008] 1 WLR 643 (noted by A. Trukhtanov, (2008) 124 LQR 364–8).

175 (1602) 5 Co Rep 117a (entire Court of Common Pleas).

176 [2007] EWCA Civ 1329; [2008] 1 WLR 643, at [42].

177 [1966] 2 QB 617, CA.

178 Referring to Law Revision Committee, *Sixth Interim Report on ‘The Statute of Frauds and the Doctrine of Consideration’* (1937, Cmd 5449).

It appears, therefore, that, when a creditor agrees to accept £90m, instead of £100m, of an outstanding debt, part-payment of the £90m (provided all of that £90m is paid) will trigger an extinction of the balance. It is not clear what is the position if the debtor pays the £90m later than the parties had agreed in their decreasing pact. Nor is it clear what is the position if the decreasing pact provides that the £90m is to be paid in tranches of £10m, for each of the next nine months, and the debtor fails to pay, say, the last tranche of £10m. At that point, is the protection of promissory estoppel forfeited so that he now owes £20m (the originally released top slice of £10m now coming back into the reckoning)? This is not discussed in the *Collier* case, although Arden LJ did state (see the quotation above) that the rescheduled part-payment must be paid 'in full'. If so, in the example just given, the answer would be: the debtor's failure to pay the last tranche renders him liable for the *whole* of the original debt (and therefore £20m is now owing, because he has in fact paid only £80m of the original £100m, and promissory estoppel's protection is contingent on the debtor adhering to the terms of the decreasing pact).

More generally, there are various problems facing 'the Denning/Arden extinction thesis', and these might be addressed if, in another case, the point arises before the Supreme Court. These problems are as follows:

- (1) As a matter of principle (5.47), it is debatable whether gratuitous debt-releasing concessions should be readily upheld, in the absence of some compelling factor, such as the risk of great hardship to the debtor. Such a gratuitous release would diminish the assets of the creditor, including assets available to his trustee in bankruptcy or to his liquidator.
- (2) 'Extinction' of the creditor's rights in equity under the *High Trees* doctrine would involve a drastic clash between common law and equity. Equitable estoppel is being used to trump the rule in *Pinnel's Case*.
- (3) The sequence of nineteenth-century House of Lords precedents was the 'wrong way round' for the purpose of Denning J's *dictum* in the *High Trees* case: *Foakes v. Beer* (1884) (5.46 and 5.48), which ratified the common law rule in *Pinnel's Case* (5.45) was decided after *Hughes v. Metropolitan Railway* (1877). And yet the House of Lords in *Foakes v. Beer* made no reference at all to the equitable doctrine, a remarkable omission.
- (4) It is submitted that the judges in the *Collier* case (2007)¹⁷⁹ were too quick, and arguably mistaken, to interpret the *D & C Builders* case¹⁸⁰ as a two-judge affirmation of Lord Denning's 'extinction' thesis (admittedly, Danckwerts LJ referred to the absence of equitable factors in favour of Mrs Rees;¹⁸¹ but otherwise he does not specifically address Lord Denning's analysis of promissory estoppel; the third judge, Winn LJ, decided the case solely by reference to common law principles, that is, the rule in *Pinnel's Case*). However, it appears that only the Supreme Court will

¹⁷⁹ [2007] EWCA Civ 1329; [2008] 1 WLR 643.

¹⁸⁰ [1966] 2 QB 617, CA.

¹⁸¹ *Ibid.*, at 625–7.

be able to re-open this aspect of the *Collier* case. Until that happens, English law is settled.

- (5) It is debatable whether the mere fact of part-payment should be sufficient to satisfy the requirement of 'reliance'. Part-payment is not an intrinsically detrimental act, because it is made in pursuance of a subsisting legal obligation. The *Collier* decision on this point adopts, therefore, a very generous approach to the notion of sufficient reliance. The Supreme Court might prefer, in a future case, to revisit this generous approach and require a stronger element of reliance.
- (6) Nor is it clear that reliance in this context can only be constituted by part-payment, despite the suggestion in the *Collier* case. Suppose that a creditor states that for the next quarter he will reduce a tenant's rent from £50,000 to £20,000. In reliance on this, the tenant, *ahead of the relevant quarter date*, spends the supposedly released portion of £30,000 on training for its staff. Staff training is an innovation in the tenant company. The *Collier* decision would appear (5.60) not to regard this as reliance effective to extinguish the balance of the next quarter's payment. But pre-*Collier* judicial discussion had indicated that irreversible detrimental reliance (other than part-payment itself) would be capable of extinguishing the relevant part of the debt: Lord Hodson in *Ajayi v. Briscoe* (1964)¹⁸² suggested that 'the [creditor's] promise only becomes final and irrevocable if the promisee cannot resume his position'. It is submitted that reliance should not, therefore, be confined to acts of part-payment.
- (7) Indeed, reliance, for the purpose of this doctrine, needs to be strong enough, according to earlier case law, to warrant equity's protection of the representee. This point is related to the next issue (see (8) below). Thus, although the essence of estoppel is that the representee *relies* on the other party's statement, Goff J in '*The Post Chaser*' (1982) held that the court can decide that there is *insufficient* reliance to justify estoppel.¹⁸³
- (8) Finally, Longmore LJ's judgment in the *Collier* case states that, in addition to reliance, the court must be convinced that it is equitable, that is, fair in all the circumstances, that estoppel should apply. By contrast, Arden LJ's analysis appears to eliminate this further requirement, by adopting the view that reliance by part-payment is enough and that, thereupon, the creditor cannot resile from his promise to accept part-payment.¹⁸⁴ Arden LJ's approach is mechanistic. By contrast, Longmore LJ suggests that the court has an opportunity to assess whether it would be inequitable for the creditor to resile *even if there has been some reliance* by the debtor. He said:¹⁸⁵ 'There is then a third question, namely whether it would be inequitable for the company to resile from its promise. That cannot be inquired into on this appeal, but I agree that it is arguable that it would be inequitable. There might, however, be much to

182 [1964] 1 WLR 1326, PC; a view favoured by *Treitel* (12th edn, London, 2007), 3–116 (at least prior to the decision in *Collier v. Wright* (2007)).

183 '*The Post Chaser*' [1982] 1 All ER 19, 25B–27, Goff J (representee's reliance insufficient).

184 [2007] EWCA Civ 1329; [2008] 1 WLR 643, at [42].

185 *Ibid.*, at [48], *per* Longmore LJ.

be said on the other side.' The fact that the creditor has been exposed to duress or fraud would render it not inequitable for him to insist on his strict legal rights. But, even where fraud or duress does not preclude resort to this estoppel, the courts will continue to weigh the suggested reliance to determine whether, or to what extent, the creditor should be estopped from enforcing those strict legal rights.¹⁸⁶

5.61 *Promissory estoppel not a cause of action.*¹⁸⁷ In *Combe v. Combe* (1951), the Court of Appeal, including Denning LJ, held that promissory estoppel operates as a shield and not a sword.¹⁸⁸ It does not establish an independent cause of action. It merely furnishes a defence. Unrequested detrimental reliance on another's promises does not generate a contract: consideration (or a deed) must be shown to support the *initial contract*.¹⁸⁹ Denning LJ's statement in this case is crystal clear:¹⁹⁰

Much as I am inclined to favour the principle stated in the *High Trees* case, it is important that it should not be stretched too far, lest it should be endangered. That principle does not create new causes of action where none existed before. It only prevents a party from insisting upon his strict legal rights, when it would be unjust to allow him to enforce them, having regard to the dealings which have taken place between the parties. That is the way it was put in *Hughes v. Metropolitan Railway*, the case in the House of Lords in which the principle was first stated ... It is also implicit in all the modern cases in which the principle has been developed ...

Seeing that the principle never stands alone as giving a cause of action in itself, it can never do away with the necessity of consideration when that is an essential part of the cause of action. The doctrine of consideration is too firmly fixed to be overthrown by a side-wind. Its ill-effects have been largely mitigated of late, but it still remains a cardinal necessity of the formation of a contract, though not of its modification or discharge.

And so *promissory* estoppel in England is not a substitute for consideration to support such an initial promise. The contrast is with *proprietary* estoppel which can be a cause of action (on which see 5.64), as in *Crabb v. Arun District Council* (1976).¹⁹¹ The English Court of Appeal in *Baird Textile Holdings Ltd v. Marks and Spencer plc* (2001)¹⁹²

186 'The Post Chaser' [1982] 1 All ER 19, 25B–27, Goff J (representee's reliance insufficient).

187 R. Halson, *Contract Law* (London, 2001), 370–85; A. Robertson, 'Estoppels and Rights-Creating Events ...', in J. W. Neyers, R. Bronaugh and S. G. A. Pitel (eds.), *Exploring Contract Law* (Oxford, 2009), 199 ff.

188 [1951] 2 KB 215, CA.

189 In England (as distinct from the USA), an agreement to give money to a charity does not become binding merely because the charity detrimentally relies on the promise: *Re Hudson* (1885) 54 LJ Ch 811, Pearson J; *Re Cory* (1912) 29 TLR 18, Eve J; cf in the USA, an informal promise to subscribe to charity is enforceable once the promisee has relied upon it: see *Restatement of the Law Second, Contracts*, section 90(2).

190 [1951] 2 KB 215, 219–20, CA.

191 [1976] Ch 179, CA.

192 [2001] EWCA Civ 274; [2002] 1 All ER (Comm) 737, CA, at [35] to [39], per Morritt LJ, and [54], per Judge LJ; similarly, *Newport City Council v. Charles* [2008] EWCA Civ 1541; [2009] WLR 1884, at [23], last sentence, per Laws LJ.

confirmed the *Combe v. Combe* restriction (the same limitation applies to the doctrine of estoppel by convention, on which see 5.68 ff below). Lord Walker in *Cobbe v. Yeoman's Row Management Ltd* (2008)¹⁹³ cited the *Baird* case without disapproval. He made clear that he was hostile to an expansion of estoppel, fearing that it would produce commercial uncertainty¹⁹⁴ (see the quotations at 5.66; the *Baird* case is further examined at 6.13).

However, the High Court of Australia in *Walton's Stores (Interstate) v. Maher* (1988) has rejected the *Combe v. Combe* restriction.¹⁹⁵ And so the Australian court has expanded the principle of protecting detrimental reliance beyond the limits of the English doctrine of proprietary estoppel (on which see 5.64). But, in England, only proprietary estoppel can operate as a cause of action.

The Australian decision in *Walton's Stores (Interstate) v. Maher* (1988)¹⁹⁶ concerned negotiations for a property development. The claimant intended to develop its own land by granting a lease of land to the defendant company and then to demolish the existing structures and build to the defendant's specifications. There was extreme urgency, and the claimant jumped the gun and began to demolish before contract terms were agreed. The defendant told its solicitors to 'go slow' in dealing with the legal documentation. The defendant became aware of the demolition work but did nothing for over one month thereafter. The defendant later withdrew from the project when the claimant had completed nearly half the building work. The High Court of Australia held that the claimant had rightly assumed that completion of the formalities of the lease would proceed smoothly. The defendant had acted unconscionably in encouraging an expectation or assumption on the part of the claimant that a contract would come into existence. The claimant had acted to his detriment to the knowledge of the defendant. Basing itself on a broad principle of estoppel, the court awarded the claimant damages in lieu of specific performance.

The English doctrine of proprietary estoppel would not be available on the facts of the *Walton's Stores* case. This is because that doctrine is restricted to the case where expenditure is incurred by a claimant on the defendant's land in the expectation that the claimant will acquire rights over the defendant's land, or on the assumption that the claimant already has such rights over the defendant's land. In the *Walton's Stores* case, the expenditure was incurred by the claimant in respect of his own land in the expectation that he would be developing it for the defendant's eventual use as a prospective tenant of the property.

193 [2008] UKHL 55; [2008] 1 WLR 1752, at [85] (noted by J. Getzler, (2009) 125 LQR 196).

194 *Ibid.*, at [46] and [81], *per* Lord Walker.

195 (1988) 164 CLR 387 (High Court of Australia); *Anson's Law of Contract* (29th edn, Oxford, 2010), 124 ff; R. Halson, *Contract Law* (London, 2001), 375–80; M. Spence, *Protecting Reliance* (Oxford, 1999), *passim*, advocates an expansive estoppel doctrine, especially in light of the leading Australian cases on estoppel, *Waltons Stores (Interstate) Ltd v. Maher* (1988) 164 CLR 387, and *Commonwealth of Australia v. Verwayen* (1990) 170 CLR 394; criticised by Peter Jaffey (book review) [2000] *Restitution Law Review* 458–64.

196 (1988) 164 CLR 387 (High Court of Australia).

It would be different if, in order to relocate his premises for the convenience of B, A enters into a matching set of informal agreements (1) to sell his property to B, and to replace this with property (2) to be bought by A from B. On such facts, Woolf J held in the English decision, *Salvation Army Trustee Co. Ltd v. West Yorkshire Metropolitan County Council* (1980)¹⁹⁷ that the purchase by A from B at stage (2) precluded B from resiling from the agreement at stage (1). An estoppel will arise in favour of A and broad justice can then be worked out (A was in fact awarded compensation in respect of B's failure to buy the old site).

5.62 True meaning of the *Combe v. Combe* restriction. However, estoppel by representation and promissory estoppel can be used by a claimant in England to overcome *some other impediment* to his claim. As Robert Goff J explained in *Amalgamated Investment & Property Co. Ltd v. Texas Commerce International Bank Ltd* (1981),¹⁹⁸ these types of estoppel can assist a claimant to make good his claim, but only by *supplementing* a basic cause of action rooted in the provision of consideration or founded perhaps on a deed (for the second of these situations, see *Shah v. Shah* (2001),¹⁹⁹ examined in detail at 5.04). It should be noted, however, that proprietary estoppel (5.64) can be used as an independent cause of action. But proprietary estoppel is confined to situations where the representee has been induced detrimentally to rely in the belief that *he has, or will shortly acquire, rights in, or in respect of, the representor's land* (or the representor has unconscionably acquiesced in that misunderstanding).

5.63 Summary of decreasing pacts

- (1) The rule in *Pinnel's Case* (1602)²⁰⁰ states that a promise to accept part-payment as full discharge is *prima facie* ineffective at common law. This can be supported on the basis that the creditor's promise is a promissory gift of a valuable asset (the benefit of a binding debt). There are exceptions if the agreement to accept part-payment is clothed as a deed or if 'fresh consideration' is provided, at the creditor's request, such as accelerated payment.
- (2) According to the Court of Appeal in the *Collier* case (2007),²⁰¹ the equitable doctrine of promissory estoppel can be used to render a debtor, if necessary, immune from liability to pay the balance of a debt. This 'extinctive' aspect of the doctrine will apply if the creditor has received part-payment following his clear promise to reduce or cancel the debt. This victory of equity over the common law rule in *Pinnel's Case*

197 *Salvation Army Trustee Co. Ltd v. West Yorkshire Metropolitan County Council* (1980) 41 P & CR 179, Woolf J; cf *Western Fish Products Ltd v. Penwith District Council* [1981] 2 All ER 204, CA (P spending money on *his own land* in expectation of receiving planning permission from D; no proprietary estoppel since P is not expecting that he has, or will have, any interest in D's land).

198 [1981] 1 All ER 923, 936–7; and Brandon LJ in the Court of Appeal agreed.

199 [2001] EWCA Civ 527; [2002] QB 35, at [30] to [33], *per* Pill LJ.

200 (1602) 5 Co Rep 117a (entire Court of Common Pleas); rule affirmed in *Foakes v. Beer* (1884) 9 App Cas 605, HL.

201 [2007] EWCA Civ 1329; [2008] 1 WLR 643.

- vindicates Denning J's famous *dictum* in the *High Trees* case.²⁰² Controversially, however, the *Collier* case (2007) finds solid support for promissory estoppel's suggested 'extinctive' operation in the Court of Appeal's decision in the *D & C Builders* case (1966).²⁰³ However, although the *Collier* decision might have proceeded on a misreading of the authority of the *D & C Builders* case, the law on this point is now settled by the 2007 decision in the *Collier* case, and only the Supreme Court (or the legislator) can change the law.
- (3) A person seeking equitable relief must not have acted unmeritoriously ('she who comes to equity must come with clean hands'). Lord Denning MR held that this was problematic for the debtor, Mrs Rees, in the *D & C Builders* case. The fact that she had unconscionably coerced the builder-creditor into accepting less than the full loaf was enough to bar her from invoking the equitable protection of promissory estoppel.²⁰⁴
 - (4) Although, in England, promissory estoppel or estoppel by representation is not a substitute for consideration (see point (5) below), these doctrines can assist a claimant by overcoming a bar to a cause of action founded on an independent ground, namely, consideration or deed (for example, *Shah v. Shah*).²⁰⁵
 - (5) Promissory estoppel in England is not an independent cause of action, and so it has not abolished the requirement of consideration to support the main contract: *Combe v. Combe* (1951),²⁰⁶ affirmed in the *Baird* case (2001).²⁰⁷ This is in contrast to the willingness in Australia to provide a cause of action in favour of the representee who has detrimentally relied (see 5.61 for a summary of the High Court of Australia's decision in the *Walton's Stores* case);²⁰⁸ and, even in England, proprietary estoppel (5.64 ff) is an independent cause of action, but it is confined to situations where the representee has been led to believe that he has, or will shortly acquire, rights in, or in respect of, the representor's land, or the representor has unconscionably acquiesced in that misunderstanding.

12. PROPRIETARY ESTOPPEL²⁰⁹

5.64 As mentioned at 5.01, there are three ways in which a promise can be 'upheld'. We now come to the third: that the other party has detrimentally relied on the defendant's promise

202 *Central London Property Trust Ltd v. High Trees House Ltd* [1947] 1 KB 130, 133–5.

203 [1966] 2 QB 617, CA.

204 *Ibid.*, at 625.

205 [2001] EWCA Civ 527; [2002] QB 35, at [30] to [33].

206 [1951] 2 KB 215, CA.

207 [2001] EWCA Civ 274; [2002] 1 All ER (Comm) 737, at [35] to [39], and [54]; and implicitly affirmed in *Thorner v. Major* [2009] UKHL 18; [2009] 1 WLR 776, at [61].

208 (1988) 164 CLR 387 (High Court of Australia).

209 Lord Neuberger, 'The Stuffing of Minerva's Owl? Taxonomy and Taxidermy in Equity' [2009] CLJ 437–49; M. Dixon, 'Confining and Defining Proprietary Estoppel: The Role of Unconscionability' (2010) 30 LS 408; P. Birks, G. Battersby and P. Critchley, in S. Bright and J. Dewar (eds.), *Land Law: Themes and Perspectives* (Oxford, 1998), chapters 18, 19, 20, especially at 482–5 and 496–505; S. Gardner, (1999) 115 LQR 438; A. Robertson, 'Estoppels and Rights-Creating Events ...', in J. W. Neyers, R. Bronaugh and S. G. A. Pitel (eds.), *Exploring Contract Law* (Oxford, 2009), 199 ff.

or assurance; here, there is no need to show that the detriment *was requested by the defendant*; and so the element of bargained-for detriment is often absent in this context. The factor of induced (albeit unrequested) reliance is crucial if the promise has not been given as a 'deed' (on which see 5.03 ff); nor is there a valid agreement supported by consideration. In the absence of a deed and 'consideration', proprietary estoppel, an equitable doctrine, might rescue a claimant (see 5.72 below for a summary of the types of estoppel). It is an exception to the general unenforceability of gratuitous promises (on which see 5.10 ff). It can give effect to informal promises, to the extent that the case demands, by protecting a person's detrimental reliance concerning his supposed or anticipated rights over the other party's land.²¹⁰

5.65 The House of Lords in *Cobbe v. Yeoman's Row Management Ltd* (2008) reviewed the doctrine of proprietary estoppel.²¹¹ Lords Scott and Walker examined the leading cases. This decision supports the following points:

- (1) In the context of dealing affecting or concerning land, proprietary estoppel can arise in either of these ways:²¹² A spends money improving (or otherwise²¹³ acts to his detriment *vis-à-vis*) B's land in the mistaken assumption that A has, or will acquire, rights in that land: and either:
 - (a) B makes a representation which induces that error; or
 - (b) B acquiesces (or even if B, at that point, shares A's error, but perhaps B also makes representations which fortify A's belief)²¹⁴ in A's error.
- (2) If the court finds that the estoppel is engaged on particular facts, the court has a wide discretion to award an appropriate remedy. That remedy is not confined to merely compensating the claimant for his detrimental reliance.

5.66 The following three cases illustrate the operation of proprietary estoppel. These decisions reveal the element of strong 'remedial discretion' in this context.²¹⁵

(1) In *Dillwyn v. Llewellyn* (1862), the House of Lords used proprietary estoppel to justify an award in favour of a son of his father's property. At great expense, the son had constructed property after the father had informally encouraged the belief that the son would receive title to the property.²¹⁶

210 For a summary: *Thorner v. Major* [2009] UKHL 18; [2009] 1 WLR 776, at [15], [29] and [72]; *Gillett v. Holt* [2001] Ch 210, 225C–D, 232A–F, 235E–F, CA; other leading decisions: *Crabb v. Arun District Council* [1976] Ch 179, CA (noted by P. S. Atiyah, (1976) 92 LQR 174; and by P. Millett, (1976) 92 LQR 342); *Taylor Fashions Ltd v. Liverpool Victoria Trustee Co. Ltd* [1982] QB 133, 153, Oliver J; and, for a recent application of this doctrine, see *Henry v. Henry* [2010] UKPC 3; [2010] 1 All ER 988.

211 [2008] UKHL 55; [2008] 1 WLR 1752 (noted by J. Getzler, (2009) 125 LQR 196; and by B. McFarlane and A. Robertson, 'The Death of Proprietary Estoppel' [2008] LMCLQ 449).

212 *Taylor Fashions v. Liverpool Victoria Trustees Co. Ltd* [1982] QB 133 (note).

213 *Greasley v. Cooke* [1980] 1 WLR 1306, CA (domestic services).

214 *Taylor Fashions Ltd v. Liverpool Victoria Trustee Co. Ltd* [1982] QB 133, 153.

215 S. Gardner, (1999) 115 LQR 438.

216 (1862) 4 De G F & J 517, HL.

(2) In *Cobbe v. Yeoman's Row Management Ltd* (2008),²¹⁷ the House of Lords held that no proprietary estoppel was established because the claimant could not show that he had justifiably relied on the defendant's assurance concerning a development project (reversing both the courts below). The parties to an unwritten residential development scheme failed ultimately to agree on the developer's remuneration. He had incurred expense in procuring planning permission for the development. But the informality of the agreement, and the manifest risk incurred by the developer, made it unjust to award him any proprietary interest in the landowner's property (see also Lord Scott's summary of the facts).²¹⁸ The House of Lords emphasised that Cobbe, the representee, had decided to pursue the application for planning permission knowing full well that there was no binding contract. As Lord Scott said:²¹⁹

It would be an unusually unsophisticated negotiator who was not well aware that oral agreements relating to such an acquisition are by statute unenforceable ... Cobbe was an experienced property developer ... He did not spend his money and time on the planning application in the mistaken belief that the agreement was legally enforceable. He [was] well aware that it was not.

Although these facts did not justify imposing a proprietary remedy, the House of Lords held that he should receive '*in personam* restitutionary relief'. The parties had not expected him to carry out this work without payment. A *quantum meruit* award would ensure that the defendant could not take advantage, without payment, of the benefit of the other party's services and of the planning permission which those services had produced.

(3) In *Thorner v. Major* (2009), the House of Lords upheld the trial judge's decision that proprietary estoppel arose on the following facts.²²⁰ The claimant had worked for nineteen years for free on the defendant estate's farm. The latter had given clear assurances that, after his death, the claimant would be entitled to the farm. In 1990, the owner had handed the claimant an insurance bonus notice relating to two policies on his life and said: 'That's for my death duties.' In 1997, the owner made a will in which he left legacies totalling £225,000 and the whole of his residuary estate to the claimant, who was also named as sole executor. But the will was revoked when the testator fell out with one of the legatees, someone other than the claimant. The owner did not make a new will and died intestate.

The House of Lords, agreeing with the trial judge, held that objectively there had been a clear enough set of assurances for it to have been reasonable for the claimant to feel assured that the farm would become his in due course. The Court of Appeal had been wrong to second-guess these findings of fact and the inferences drawn from the parties'

217 [2008] UKHL 55; [2008] 1 WLR 1752 (noted by J. Getzler, (2009) 125 LQR 196; and by B. McFarlane and A. Robertson, 'The Death of Proprietary Estoppel' [2008] LMCLQ 449).

218 [2008] UKHL 55; [2008] 1 WLR 1752, at [2].

219 *Ibid.*, at [27].

220 [2009] UKHL 18; [2009] 1 WLR 776 (noted by B. McFarlane and A. Robertson (2009) 125 LQR 535–42; B. Sloan, [2009] CLJ 518); applied in *Cook v. Thomas* [2010] EWCA Civ 227; [2010] All ER (D) 155.

rather primitive and implicit communications on this matter. Furthermore, the House of Lords held it did not matter that the size of the farm had varied during the course of the parties' dealings. The subject matter of the assurance remained certain enough: it was the farm and the equipment and livestock situated on it at the time of the owner's death.

- 5.67 Proprietary estoppel remains confined to situations relating to land, despite contrary *dicta*,²²¹ including Lord Scott's suggestion in *Cobbe v. Yeoman's Row Management Ltd* (2008),²²² that 'in principle' this form of estoppel should be 'equally available to chattels or choses in action'. If proprietary estoppel were to expand beyond the present context of dealings with land, this might tend to undermine the whole doctrine of consideration. Furthermore, Lord Walker in *Cobbe v. Yeoman's Row Management Ltd* (2008) indicated that he was hostile to such an expansion and fearful that it would create commercial uncertainty.²²³

Equitable estoppel is a flexible doctrine which the Court can use, in appropriate circumstances, to prevent injustice caused by the vagaries and inconstancy of human nature. But it is not a sort of joker or wild card to be used whenever the Court disapproves of the conduct of a litigant who seems to have the law on his side. Flexible though it is, the doctrine must be formulated and applied in a disciplined and principled way. Certainty is important in property transactions.

13. ESTOPPEL BY CONVENTION²²⁴

- 5.68 The Court of Appeal in *Amalgamated Investment & Property Co. Ltd (in liquidation) v. Texas Commerce International Bank Ltd* (1982)²²⁵ adopted as authoritative this passage in *Spencer Bower and Turner's Estoppel by Representation*:²²⁶

This form of estoppel is founded not on a representation of fact made by a representor and believed by a representee, but on an agreed statement of facts the truth of which has been assumed, by the convention of the parties, as the basis of a transaction which they are about to enter. When the parties have acted in their transaction upon the agreed assumption that a given state of facts is to be accepted between them as true, then as regards that transaction each will be estopped as against the other from questioning the truth of the statement of facts so assumed.

221 *Crabb v. Arun District Council* [1976] Ch 179, 193, CA, *per* Scarman LJ; *Taylor Fashions Ltd v. Liverpool Victoria Trustee Co. Ltd* [1982] QB 133, 153, *per* Oliver J; *Amalgamated Investment & Property Co. Ltd v. Texas Commerce International Bank Ltd* [1982] QB 84, 103–4, 122, *per* Robert Goff J (in the Commercial Court) and Lord Denning MR (in the Court of Appeal).

222 [2008] UKHL 55; [2008] 1 WLR 1752, at [14].

223 *Ibid.*, at [46] and [81].

224 Lord Steyn, 'Contract Law: Fulfilling the Reasonable Expectations of Honest Men' (1997) 113 LQR 433, 440; T. Dawson, (1989) 9 LS 16; K. R. Handley, *Estoppel by Conduct and Election* (London, 2006), chapter 8. On this doctrine, see also 14.06 and 14.22.

225 [1982] 1 QB 84, CA.

226 3rd edn, London, 1977, 157.

Estoppel by convention was obscure until the Court of Appeal in the *Amalgamated Investment* case (1982) resuscitated it (see 5.72 below for a summary of the types of estoppel).

In this case, the claimant had guaranteed in favour of the defendant a loan made by the latter to the claimant's subsidiary. In fact, the defendant made this loan through a subsidiary company called Portsoken, but the wording of the guarantee did not reflect this. Instead, that document declared that the claimant's guarantee was in respect of moneys paid by the defendant rather than by the defendant's subsidiary. The claimant's liquidator sought a declaration that it was not liable on the guarantee for loans made by Portsoken. The Court of Appeal cut through this knot by saying that the claimant guarantor was estopped from denying that in fact it owed money under the guarantee in respect of the true lender, Portsoken. This estoppel reflected the course of dealing between claimant and defendant.

In the Court of Appeal, the first ground of decision was that the guarantee should be interpreted, as a matter of 'construction', as extending to loans made by Portsoken (generally on the process of contractual interpretation see chapter 14). The estoppel point is perhaps a second *ratio*. (Note that, at first instance in that case, Robert Goff J dealt with the case on the basis of estoppel by representation; his judgment has been considered at 5.62 above.)

5.69 Estoppel by convention differs from the main types of estoppel, 'estoppel by representation', 'promissory estoppel' and 'proprietary estoppel' (each of these has been encountered above at 5.53, 5.54 and 5.64) because it requires *no representation*, nor is it necessary to show that one party has acquiesced in bad faith in the other's error. Instead, its essence is that the *outward course of conduct evidences or varies an agreement*.²²⁷ It requires some *pattern of visible conduct* which indicates a shared assumption.²²⁸ And no such *conduct* can arise merely from a pair of matching assumptions lodged metaphysically in the parties' minds. In *Durham v. BAI (Run Off) Ltd* (2008), Burton J said:²²⁹

The three ingredients are succinctly summarised by Bingham LJ in '*The Vistafjord*' [1988] 2 Lloyd's Law Rep 343 at 352, namely that it applies where:

'(1) parties have established by their construction of their agreement or their apprehension of its legal effect a conventional basis,

(2) on that basis they have regulated their subsequent dealings, to which I would add

(3) it would be unjust or unconscionable if one of the parties resiled from that convention.'²³⁰

227 *Republic of India v. India Steamship Co. Ltd ('The Indian Endurance')* (No. 2) [1998] AC 878, 914–15, HL, per Lord Steyn, clarifying the Court of Appeal's formulation of the doctrine.

228 *Ibid.*, at 914–15; *Bridgewater v. Griffiths* [2000] 1 WLR 524, 530, per Burton J.

229 [2008] EWHC 2692 (QB); [2009] 4 All ER 26, at [267] and [268], per Burton J.

230 The element of unconscionability was absent in the *Durham* case, [2008] EWHC 2692 (QB); [2009] 4 All ER 26, at [284], per Burton J.

As Bingham LJ points out at 351, and as he further makes clear in *'The Captain Gregos'* (No. 2) [1992] Lloyd's Law Rep 395 at 405, each party must be 'fully cognizant' of the shared assumption and 'an estoppel by convention requires communications to pass across the line between the parties'.

However, the element of sustained conduct is (understandably) absent in decisions which have *explicitly* considered non-reliance clauses (9.28). In that context, the Court of Appeal in the *Peekay* case (2006)²³¹ (9.30) invoked the (synonymous) concept of 'estoppel by contract' to explain that such a clause takes effect as a species of free-standing agreement. And so there is no need to show that there has been reliance by the representor on the representee's assertion that the latter has not relied on any possible representation.

5.70 Estoppel by convention *does not give rise to a cause of action*, but it can clear the way for a contractual, or other, cause of action to be made out.²³² Thus, the defendant bank in the *Amalgamated Investment* case (5.68) could have used the estoppel to buttress a contractual claim on the guarantee. But the estoppel would not by itself found an action: consideration must exist independently of the estoppel which evidences that agreement. This mirrors the restriction, acknowledged in *Combe v. Combe* (1951)²³³ (5.61) on the operation of both estoppel by representation and promissory estoppel.

5.71 Estoppel by convention cannot be used to circumvent a statutory prohibition upon contracting out of a protective set of rules.²³⁴

14. SUMMARY OF TYPES OF ESTOPPEL

5.72 The main types of estoppel are:

- (1) *Estoppel by representation*. This normally involves a representation by words, but sometimes it can be by non-verbal conduct, indicating that the representee should be assured that something has happened or is presently the case. *Jorden v. Money* (1854) is regarded as House of Lords authority that common law estoppel requires a representation of a past or present fact and does not extend to promises of future conduct or future abstention.²³⁵ For an illustration, see *Shah v. Shah* (2001) at 5.04.²³⁶

231 *Peekay Intermark Ltd v. Australia and New Zealand Banking Group Ltd* [2006] EWCA Civ 386; [2006] 2 Lloyd's Rep 511, at [56], [57] and [70]; applied and considered in *JP Morgan Chase Bank v. Springwell Navigation Corporation* [2008] EWHC 1186, at [556] ff, Gloster J; *Trident Turboprop (Dublin) Ltd v. First Flight Couriers* [2008] EWHC 1686; [2009] 1 All ER (Comm) 16, Aikens J, in a footnote (n. 9) (Aikens J's decision in the *Trident* case was affirmed on appeal without discussion of the point, [2009] EWCA Civ 290; [2010] QB 86); A. Trukhtanov, (2009) 125 LQR 648.

232 *Amalgamated Investment & Property* case, [1982] 1 QB 84, 132, CA, *per* Brandon LJ.

233 [1951] 2 KB 215, CA.

234 *Keen v. Holland* [1984] 1 WLR 251 (protection under the agricultural holdings legislation).

235 (1854) 5 HL Cas 185.

236 [2001] EWCA Civ 527; [2002] QB 35, at [30] to [33].

- (2) *Proprietary estoppel*. This form of estoppel is confined in England to assurances that the representee has or will acquire rights in, or over, the representor's *land*. This type of estoppel can concern the *future and is not confined to past or present* facts. The doctrine can also found a cause of action, and so it is not merely a 'shield'. The doctrine is rooted in principles of equity. Good illustrations are *Crabb v. Arun District Council* (1976)²³⁷ and *Thorner v. Major* (2009) (5.66, case (3)).²³⁸
- (3) *Promissory estoppel*. This form of estoppel has been adopted predominantly in respect of assurances that a debtor (or another person owing a subsisting obligation) will have more time or will be (or has already been) relieved from the remainder of his debt (or other obligation). This type of estoppel can concern the *future* and is not confined to *past or present* facts. However, this form of estoppel does *not* found a cause of action, but is merely a 'shield'. Promissory estoppel is rooted in principles of equity.
- (4) *Estoppel by convention*. This concerns coincident patterns of conduct (for a qualification, see 5.69 on non-reliance clauses). Such conduct can indicate that the parties have concurred in treating a subsisting transaction as having a particular effect or application, or that it is valid (5.68). This type of estoppel does not require a specific representation. It appears to be regarded as an offshoot of common law principle.
- (5) *Res judicata*. This concerns the preclusive effect of *judicial decisions between the parties*. Its effect is to bring about 'claim or issue preclusion',²³⁹ thereby preventing claims or issues from being re-litigated between the same parties.²⁴⁰ This principle also rests on notions of estoppel. *Res judicata* is considered in works on civil procedure. Estoppel by *res judicata* has three elements:
 - (i) judgments and other relevant decisions (see element (c) below) will be binding upon both parties (and their privies²⁴¹ or successors);²⁴²
 - (ii) if the judgment was made in a civil matter (a final decision,²⁴³ or consent order);²⁴⁴ and

237 [1976] Ch 179, CA (Lord Denning MR, Lawton and Scarman LJ).

238 [2009] UKHL 18; [2009] 1 WLR 776 (noted by B. McFarlane and A. Robertson, (2009) 125 LQR 535–42).

239 This terminology, current in the USA and in Canada, has been adopted in ALI/UNIDROIT's *Principles of Transnational Civil Procedure* (Cambridge, 2006), Principles 28.2 and 28.3.

240 G. Spencer Bower, A. K. Turner and K. R. Handley, *The Doctrine of Res Judicata* (3rd edn, London, 1996); N. Andrews, *The Modern Civil Process* (Tübingen, 2008), 8.22 ff.

241 *McIlkenny v. Chief Constable of the West Midlands* [1980] 1 QB 283, CA; *House of Spring Gardens Ltd v. Waite* [1991] 1 QB 241, CA; *Black v. Yates* [1992] 1 QB 526, 545–9; G. Spencer Bower, A. K. Turner and K. R. Handley, *The Doctrine of Res Judicata* (3rd edn, London, 1996), at [231] and [232].

242 E.g. *Green v. Vickers Defence Systems Ltd* [2002] EWCA Civ 904; *The Times*, 1 July 2002.

243 Including a final decision of an interim application: *R v. Governor of Brixton Prison, ex parte Osman* [1991] 1 WLR 281; *Possfund v. Diamond* [1996] 2 All ER 774, 779; for an example of a non-final decision, see *Buehler AG v. Chronos Richardson Ltd* [1998] 2 All ER 960, CA.

244 E.g. *Palmer v. Durnford Ford* [1992] 1 QB 483, Simon Tuckey QC sitting as a Deputy High Court Judge; *Green v. Vickers Defence Systems Ltd* [2002] EWCA Civ 904; *The Times*, 1 July 2002; *Gairy v. Attorney-General of Grenada* [2001] UKPC 30; [2002] 1 AC 167, at [27].

- (iii) the judgment was made by a competent civil court or tribunal,²⁴⁵ including courts recognised under English rules of private international law²⁴⁶ and arbitration proceedings.²⁴⁷

²⁴⁵ *Green v. Hampshire County Council* [1979] ICR 861; *Crown Estate Commissioners v. Dorset County Council* [1990] Ch 297, Millett J.

²⁴⁶ P. R. Barnett, *Res Judicata, Estoppel and Foreign Judgments: The Preclusive Effects of Foreign Judgments in Private International Law* (Oxford, 2001); P. Rogerson, (1998) *Civil Justice Quarterly* 91.

²⁴⁷ *Ron Jones (Burton-on-Trent) Ltd v. JS Hall* (unreported, 3 August 1999).

Chapter contents

1. Introduction *para. 6.01*
2. Foundations of the doctrine *para. 6.02*
3. The 'non-commercial' context: leading decisions *para. 6.09*
4. The 'commercial' context: leading decisions *para. 6.12*
5. Borderline of 'commercial and non-commercial' relations *para. 6.14*
6. The future *para. 6.15*

6

Intent to create legal relations

1. INTRODUCTION

6.01 Summary of main points¹

- (1) The 'intent to create legal relations' doctrine is additional to the doctrine of consideration (see chapter 5). Therefore, in the absence of a deed (5.03), if a person wishes to sue on a promise, he must overcome two hurdles: first, he must show that the promise was made in circumstances satisfying the notion of a bargain (the element of 'consideration'). Secondly, he must show that the promise was made and received in circumstances consistent with an 'intent to create legal relations'.
- (2) In the commercial sphere, there is a strong presumption that such an 'intent' goes without saying: there is, in other words, a strong presumption that a commercial agreement is intended to create legal relations, although this can be rebutted explicitly or, perhaps, if the context indicates that the parties did not in fact intend to create legally enforceable rights. In particular, parties to a commercial agreement can explicitly exclude legal relations, notably by use of the formula 'subject to contract' (6.06).
- (3) But even a commercial arrangement will be presumed to give rise to a contract only if there is a clear commitment, an 'apparent promise'. A 'letter of comfort' (that is, a parent company's vague indication of its current policy to satisfy its subsidiary's debts) does not disclose such a promise; nor will an open-ended and non-committal pattern of dealings between merchants disclose a hard-edged commitment to maintain legal relations.

¹ M. Furmston and G. J. Tolhurst, *Contract Formation: Law and Practice* (Oxford, 2010), chapter 10; M. Freeman, in R. Halson (ed.), *Exploring the Boundaries of Contract* (Aldershot, 1996), chapter 4; S. Hedley, 'Keeping Contract in its Place – Balfour v. Balfour and the Enforceability of Informal Agreements' (1985) 5 OJLS 391; B. Hepple, [1970] CLJ 122; D. Allen, (2000) *Anglo-American Law Review* 204; S. Ball, (1983) 99 LQR 572.

- (4) In certain non-commercial contexts, an agreement might not be accompanied by such an 'intent'. The leading case, *Balfour v. Balfour* (1919), concerned a maintenance arrangement between spouses who had not formally separated, but who were temporarily living apart, ostensibly still on good terms. In this and similar contexts, the courts presume that promises, even though technically supported by consideration, should remain beyond the pale of legal enforcement.
- (5) In applying the doctrine of 'intent to create legal relations' in the non-commercial sphere, the courts can take into account various practical or policy factors, including: the objective triviality of many social or domestic promises; the need to shelter many domestic or social promises from the intrusive civil process and its remedies; and the fear of excessive litigation.
- (6) At the borderline of commercial and domestic dealings, decisions during the last fifty years indicate a willingness to extend the reach of the law; for example, *Parker v. Clark* (1960)² (6.11) and *Modahl v. British Athletic Federation Ltd* (2002)³ (6.14).
- (7) As for the future, the better view is that the present doctrine cannot be eliminated in favour of a general and necessarily vague test of 'offer and acceptance'. Intent to create legal relations and consideration are likely to remain separate tests for the validity of 'simple' contracts (that is, agreements other than those made by deed, 5.03). Radical reconstitution of the tests for formation of contract can now be achieved only by statute.

S. Hedley, 'Keeping Contract in its Place – *Balfour v. Balfour* and the Enforceability of Informal Agreements' (1985) 5 OJLS 391, especially 400–4

2. FOUNDATIONS OF THE DOCTRINE

6.02 *Genesis of the doctrine.* *Carlill v. Carbolic Smoke Ball Co.* (1893) crystallised the doctrine (for the main discussion of this bizarre case, see 3.42).⁴ The Court of Appeal held that

² [1960] 1 WLR 286, Devlin J.

³ [2001] 1 EWCA Civ 1447; [2002] 1 WLR 1192, CA, at [50] to [54] and [105].

⁴ [1893] 1 QB 256 CA; A. W. B. Simpson, 'Innovation in Nineteenth Century Contract Law' (1975) 91 LQR 247, at 263–5; and A. W. B. Simpson, 'Quackery and Contract Law: The Case of the Carbolic Smoke Ball' (1985) 14 JLS 345 (the latter is reprinted in A. W. B. Simpson, *Leading Cases in the Common Law* (Oxford, 1995), chapter 10); the *Carbolic Smoke Ball* case was applied in *Bowerman v. ABTA Ltd* [1996] CLC 451, noted by G. McMeel, (1997) 113 LQR 47–9.

the *Carbolic Smoke Ball Company*'s advertisement made plain that prospective customers were intended to believe that the company was making a binding offer to pay £100 if the product did not work. Otherwise, why would the company have declared that £1,000 had been 'deposited in the Alliance Bank' as a token of its serious intent? And so, in this case, a new test of contractual enforcement emerged.

- 6.03 *Non-commercial and commercial contexts.* It is common to divide this topic into two segments, non-commercial and commercial. Family, domestic or social arrangements are presumed *not* to be intended to have legal force. But in the case of commercial arrangements, the opposite starting point prevails: promises in that context are presumptively intended to be legally binding.⁵
- 6.04 *Discovering 'intent' or its absence.* Normally, the search for intent to create legal relations is a purely objective process. It takes place without inquiring into the parties' actual beliefs. For example, in *Gould v. Gould* (1970), Lord Denning MR said that the court imputes an intention (whether in favour of or against legal enforcement) on the basis of what reasonable people would say they had done.⁶ However, in borderline cases, a more nuanced approach is adopted. The court will inquire closely into what the parties actually thought to be the case, no doubt leavening this search for 'intent to create legal relations' by imposing a test of reasonableness. This scrutiny is apparent in Devlin J's decision in *Parker v. Clark* (1960, examined at 6.11 below).⁷
- 6.05 *Rationale of the 'intent to create legal relations' doctrine.* There is a link between this doctrine and the general principle of freedom of contract (1.08). This is because the 'intent' doctrine allows the parties to contract out of the legal regime. For example, the courts will respect an explicit 'gentlemen's agreement': no legal rights are created. The House of Lords held that an explicitly 'honourable pledge' clause excluded legal rights in *Rose & Frank Co. v. Crompton Bros* (1925).⁸ This case concerned (1) an overarching import arrangement, and (2) a series of specific contracts of sale. As for (1), this was expressed to be: 'not entered into ... as a formal or legal agreement, and [it] shall not be subject to legal jurisdiction in the law courts of the United States or England'. The House of Lords held that the clear terms of this overarching import arrangement negated any legal effect. However, as for (2), *individual* contracts of sale made under its umbrella were legally binding. Both parts of this decision are clearly sound.

5 E.g. *Edwards v. Skyways Ltd* [1964] 1 WLR 349, 354–5, Megaw J (6.12); *Esso Petroleum Ltd v. Commissioners of Customs & Excise* [1976] 1 WLR 1, HL; on the latter decision, see E. McKendrick, *Contract Law: Text, Cases and Materials* (4th edn, Oxford, 2010), 287.

6 [1970] 1 QB 275, 279, CA.

7 [1960] 1 WLR 286; [1960] 1 All ER 93, Devlin J.

8 [1925] AC 445, HL; *Chitty on Contracts* (30th edn, London, 2008), 2-162 to 2-164; cf the case of a non-existent supply contract, *Baird Textile Holdings Ltd v. Marks and Spencer plc* [2001] EWCA Civ 274; [2002] 1 All ER (Comm) 737 (6.14); an 'honour clause' in a business context is effectively an exclusion clause, *Atiyah's Introduction to the Law of Contract* (6th edn, Oxford, 2005), 99–103.

6.06 Another exclusionary formula is ‘subject to contract’ (see also 1.16, 2.07, 4.21, 12.04). This phrase, common in the field of land transactions, but not peculiar to that context, manifests a shared understanding that the relevant consensus is not legally effective as a contract. Although the courts have consistently respected this phrase⁹ (Nourse J’s decision in the *Alpenstow* case (1985) was a rare exception),¹⁰ the Supreme Court in the *RTS* case (2010) (4.21) held that the parties’ conduct can indicate a joint intention to disapply the ‘subject to contract’ bar. But, for this purpose, the court will need to find clear evidence of two things: (1) that all the points of dispute have been resolved during the negotiations, and (2) that the parties have substantially performed under the intended transaction. If both these matters are shown, the court can safely infer that the parties have tacitly agreed to override an express ‘subject to contract’ clause. Another qualification is that estoppel can override the ‘subject to contract’ formula.¹¹ However, that proposition needs now to be considered against the more restrictive approach displayed by the House of Lords in commercial contexts in *Cobbe v. Yeoman’s Row Management Ltd* (2008)¹² (5.66, case (2)).¹³ Even if the phrase ‘subject to contract’ is not explicitly used, the Court of Appeal in *Grant v. Bragg* (2009)¹⁴ acknowledged that a clear requirement that an oral or e-mailed consensus should be finalised in writing (on paper) is sufficient to imply that the parties’ dealings are ‘subject to contract’. The court distinguished between a binding agreement importing a further obligation to sign a formal written instrument recording the agreement and a non-binding agreement which is capable of becoming binding only if the parties sign or agree written terms. The Court of Appeal rejected the trial judge’s view that the parties’ e-mail correspondence indicated that they were free to achieve a binding agreement without complying with the formal signing of the draft written agreement.

6.07 A variation on the theme of ‘freedom of contract’ (1.08) is the position regarding a collective agreement (a consensus between a trade union and an employer). Statute states that such an agreement is presumed to be *unenforceable* unless the parties explicitly declare otherwise.¹⁵ In that special context, therefore, the law allows the parties to

9 Decisions respecting ‘subject to contract’ are legion: *Winn v. Bull* (1877) 7 Ch D 29; *Chillingworth v. Esche* [1924] 1 Ch 97, CA; *Regalian Properties plc v. London Dockland Development Corporation* [1995] 1 WLR 212, Rattee J, noted by Key, (1995) 111 LQR 576; E. McKendrick, [1995] *Restitution Law Review* 100.

10 *Alpenstow Ltd v. Regalian Properties Ltd* [1985] 1 WLR 721, Nourse J, noted by C. Harpum, [1985] CLJ 356, emphasising the decision’s very exceptional features.

11 *Salvation Army Trustee Co. Ltd v. West Yorkshire Metropolitan County Council* (1980) 41 P & CR 179, approved but distinguished in *Attorney-General of Hong Kong v. Humphreys Estates (Queens Gardens) Ltd* [1987] 1 AC 114, 127, PC; for an Australian decision, see *Waltons Stores (Interstate) Ltd v. Maher* (1988) 76 ALJ 513 (High Court of Australia); on these decisions, see R. Goff and G. H. Jones, *The Law of Restitution* (7th edn, 2007), 26-012 to 26-014.

12 [2008] UKHL 55; [2008] NPC 95, at [14].

13 Collateral warranties can arise even though the main contract is ‘subject to contract’: *Business Environment Bow Lane Ltd v. Deanwater Estates Ltd* [2007] EWCA Civ 622; [2007] L & TR 26 (although such a warranty was not found on the facts: see 9.11 ff). ‘Lock out’ agreements for a specified period can also be created, even though the main contract is ‘subject to contract’: *Pitt v. PHH Asset Management Ltd* [1994] 1 WLR 327, CA (2.07).

14 [2009] EWCA Civ 1228; [2010] 1 All ER (Comm) 1166, at [28] to [32], *per* Lord Neuberger MR.

15 Section 179 of the Trade Union and Labour Relations (Consolidation) Act 1992.

contract *into* the sphere of legal enforceability; otherwise the collective agreement has no legal effect.

- 6.08 *A filter upon agreements which legally 'count'*. The 'intent to create legal relations' doctrine also affords the courts an opportunity to take into account various practical or policy factors. The result is that the 'intent' doctrine can be used to deny legal effect to technical bargains: such arrangements would be enforceable if consideration alone determined the question of enforceability (see 6.16 ff for discussion of that doctrinal interaction). Three main factors are discernible in the cases (for example, *Balfour v. Balfour* (1919), discussed more fully at 6.09).¹⁶ First, there is the objective triviality of many social or domestic promises. As Warrington LJ said: '[I]f we were to hold that there was a contract in this case we should have to hold that with regard to all the more or less trivial concerns of life where a wife, at the request of her husband, makes a promise to him, that is a promise which can be enforced in law.'¹⁷ Secondly, it would be inappropriate for domestic or social promises to be subject to the heavy-handed and intrusive process and remedies of the commercial system of contract. As Atkin LJ said: 'The common law does not regulate the form of agreements between spouses ... The consideration that really obtains for them is that natural love and affection which counts for so little in these cold Courts ... In respect of these promises each house is a domain into which the King's writ does not seek to run, and to which his officers do not seek to be admitted.'¹⁸ Thirdly, there is the obvious fear of excessive litigation if every technical 'bargain', however informal or trivial, were capable of being sued upon. As Atkin LJ said (in a passage which is quoted at greater length in the next paragraph): 'All I can say is that the small Courts of this country would have to be multiplied one hundredfold if these arrangements were held to result in legal obligations.'¹⁹

3. THE 'NON-COMMERCIAL' CONTEXT: LEADING DECISIONS

- 6.09 *Bargains between spouses while the marriage remains harmonious*. *Balfour v. Balfour* (1919) contains a famous endorsement by the Court of Appeal of the 'intent to create legal relations' doctrine in the matrimonial context. Atkin LJ, in a characteristically purple passage (cited above at 6.08), said that the cold courts are no place for spouses to sue each other for breach of promises if, at the time of the relevant contract's formation, they were living 'in amity':²⁰

All I can say is that the small Courts of this country would have to be multiplied one hundredfold if these arrangements were held to result in legal obligations. They are

¹⁶ [1919] 2 KB 571, CA.

¹⁷ *Ibid.*, at 575, *per* Warrington LJ.

¹⁸ *Ibid.*, at 579, *per* Atkin LJ; M. Freeman, in R. Halson (ed.), *Exploring the Boundaries of Contract* (Aldershot, 1996), chapter 4, suggests that this is a doubtful point in the modern atomistic age, although J. O'Sullivan and J. Hilliard, *The Law of Contract* (4th edn, Oxford, 2010), 3.8, think the point is valuable.

¹⁹ [1919] 2 KB 571, 577, 579, CA, *per* Duke LJ and Atkin LJ.

²⁰ *Ibid.*, at 579; the formula of 'in amity' recurs at 572 and 576.

not sued upon, not because the parties are reluctant to enforce their legal rights when the agreement is broken, but because the parties, in the inception of the arrangement, never intended that they should be sued upon. Agreements such as these are outside the realm of contracts altogether. The common law does not regulate the form of agreements between spouses. Their promises are not sealed with seals and sealing wax. The consideration that really obtains for them is that natural love and affection which counts for so little in these cold Courts. The terms may be repudiated, varied or renewed as performance proceeds or as disagreements develop, and the principles of the common law as to exoneration and discharge and accord and satisfaction are such as find no place in the domestic code. The parties themselves are advocates, judges, Courts, sheriff's officer and reporter. In respect of these promises each house is a domain into which the King's writ does not seek to run, and to which his officers do not seek to be admitted.

On the present facts, the Balfours' marriage had been still intact when they agreed these maintenance payments. And so, at that stage they had not been bargaining at arm's length in the manner of estranged spouses or former partners.

Mr Balfour was an irrigation engineer from Ceylon. He and his wife had settled briefly in England. Nine months later, he returned to his job in Ceylon, to continue his job there. The wife remained in England recuperating from rheumatoid arthritis. Her husband promised to pay her £30 per month during their enforced but ostensibly amicable separation. At this stage, they were physically separated but the marriage was intact. However, two years later, Mrs Balfour obtained a decree nisi. At this stage, she also obtained an order for maintenance. She then sued for the unpaid payments under the pre-divorce maintenance agreement. At trial, Sargant J upheld the wife's claim. He found both consideration and 'intent to create legal relations'. (The promise made by the wife would appear to be the implicit undertaking not to pledge the husband's credit for more than the £30 per month which he had promised to pay.)

But the Court of Appeal reversed on the second point and so the action failed (and Warrington and Duke LJ considered²¹ that there was no real counter-promise by the wife, and hence no consideration). The Balfours' marriage had still been intact when they agreed these maintenance payments. The decision declares, therefore, that law should not enforce such a marital promise or bargain, even if there had been consideration, if the parties were not estranged at the time of the contract's formation.

Balfour v. Balfour negatives promises between spouses, even where consideration is present, only if the promise is made while the marriage is harmonious, or at least the parties are not voluntarily separated, one or both having chosen to live apart. It was on this basis that the decision was convincingly distinguished by the Court of Appeal in *Merritt v.*

²¹ *Ibid.*, at 575, 577–8, respectively.

Merritt (1970).²² In that case a husband had left his wife for another woman. Before doing so, his wife insisted that he write down his promise that the wife would become solely entitled to the matrimonial home if she paid off the remaining mortgage instalments. He also promised her a sum as maintenance. All three Court of Appeal judges latched on to the fact that, unlike *Balfour v. Balfour*, it was manifest in this case that the Merritts' marriage was 'on the rocks'. The court issued a declaration that the property should now be transferred from their joint names into the wife's sole name. In the *Merritt* case, Widgery LJ expressed this as follows: 'The experience of life and human nature which raises this presumption in the case of a husband and wife living together in amity does not support it when the affection which produces that relationship of confidence has gone.'

The *Balfour* case (1919) is often cited for the broad proposition that most types of family financial contracts are legally unenforceable. But this perception of social expectations is open to question. A strong presumption against legal enforcement might no longer be appropriate. Perhaps even agreements between spouses while the marriage is emotionally sound might be accorded enforcement.²³ In any event, a deed will seal matters in favour of enforcement (in the absence of misrepresentation, duress, or undue influence). Baroness Hale acknowledged this last point in *Granatino v. Radmacher* (2010), where she said:²⁴

There is nothing to stop a husband and wife from making legally binding arrangements, whether by contract or settlement, to regulate their property and affairs while they are still together ... These days, the commonest example of this is an agreement to share the ownership or tenancy of the matrimonial home, bank accounts, savings or other assets. Agreements for housekeeping or personal allowances, on the other hand, might run into difficulties. In *Balfour v. Balfour* [1919] 2 KB 571, a husband agreed to pay his wife £30 per month when he returned to his work in Ceylon while she remained in England for medical reasons. Duke LJ doubted whether the wife had given consideration for the husband's promise. Atkin LJ would have had no difficulty in finding that her promise to spend the money for its intended purposes was consideration, but held, at p. 579, that the couple had never intended that the arrangement should have contractual force: "the small courts of this country would have to be multiplied one hundredfold if these arrangements were held to result in legal obligations." But any problems posed by the doctrine of consideration or the need to express contractual intent could be solved by making the agreement by deed.

6.10 Other family arrangements: mother retracting daughter's 'start up' accommodation. *Jones v. Padavatton* (1969) is another case often cited as supporting the presumption that family arrangements are unenforceable.²⁵ However, only Danckwerts LJ invoked

22 [1970] 1 WLR 1211, 1214, CA.

23 E. McKendrick, *Contract Law: Text, Cases and Materials* (4th edn, Oxford, 2010), 282, reviews the literature on this.

24 [2010] UKSC 42; [2010] 3 WLR 1367, at [142]. For developments concerning ante-nuptial agreements, see 20.13.

25 [1969] 1 All ER 328, CA.

this presumption. The other two members of the three-judge court agreed on the result but adopted different lines of reasoning.

In 1962, a mother persuaded her divorced daughter, aged 34, to leave her job in Washington DC, go to London and read for the English Bar, with a view to eventual practice in the West Indies. The mother promised to provide maintenance for her period of legal study. In 1964, the agreement was varied: instead of maintenance, the daughter could reside in a house which the mother had bought. The house remained in the mother's name. The parties had not specified a time limit on the daughter's entitlement to remain in the house. In 1967, the daughter was 39, and had not yet passed her exams. The mother and daughter then fell out. The legal issue was whether she could now evict the daughter, or could the daughter claim that she had a contractual right to stay?

The Court of Appeal unanimously held that the daughter did not have a contractual right to stay. Only Danckwerts LJ adopted the presumption, deduced from the *Balfour* case (1919) (6.09), against enforcement of 'family arrangements'. The other two judgments, by Fenton-Atkinson and Salmon LJ, instead display a sensitive appreciation of the particular facts, rather than resort to a mechanical presumption (Fenton-Atkinson LJ finding no intention to create legal relations on the facts and Salmon LJ finding that a valid contract had existed but it had now expired).

- 6.11 *Friends sharing accommodation: a storm in Torquay*. In *Parker v. Clark* (1960),²⁶ Devlin J upheld as legally enforceable a promise between friends to reward a party for 'support services' by a share of the benefited party's estate.

The claimants, a couple in their fifties, agreed to sell their house ('The Thimble') and to move in with the defendants, a couple in their late seventies. The claimants and defendants were not related. The claimants also agreed to share many of the outgoings on the property. In return, the defendants promised to accommodate the couple and to leave them a one-third share of the value of their estate when they had both died. The arrangement, only partly recorded in writing, was then implemented. There was a year and a half of contented cohabitation. Then, after a decline in relations, the defendants evicted the claimants, and the latter sued successfully for damages in respect of 'loss of bargain'.

The judge's award of £4,600 consisted of two elements: (1) loss of rent-free accommodation, use of the defendants' car and a television set (these items of loss being reckoned at £300 a year, with a 'multiplier' of four years, and so the sum awarded under this first heading was £1,200); and (2) loss of the promised one-third share of the defendants' real estate (valued at £3,400).

26 [1960] 1 All ER 93, Devlin J; see also *Gillett v. Holt* [2001] Ch 210, CA (reviewing cases on proprietary estoppel claims concerning promises to leave the claimant property in promisor's will in return for the claimant's future domestic services etc. performed by the promisee in the promisor's lifetime).

Amongst many other rejected defences, Devlin J dismissed the defence based on the alleged lack of 'intent to create legal relations' because this was not a mere domestic arrangement. Therefore, *Balfour v. Balfour* (1919) (6.09) did not preclude legal enforcement.

Other cases of relevance are as follows: in *Lens v. Devonshire Club* (1914), Scrutton J refused an action by a golfer for a prize promised by his club.²⁷ In *Simpkins v. Puy*s (1955), a tripartite arrangement to participate in a weekly newspaper competition produced winnings for the defendant. Sellers J held that the other two contributors to the entry fee were each entitled to a one-third share of the winnings. In *Coward v. Motor Insurers Bureau* (1963), the Court of Appeal held that a workman providing a lift on a motorbike to a colleague, the latter making a petrol contribution, did not involve a legal contract (the point was relevant because the MIB would not be liable unless there was a contract of carriage for hire or reward). But, in *Albert v. Motor Insurers Bureau* (1972), the latter decision was doubted by Lord Cross. He considered that, although there was no joint 'intent' in the *Albert* case that a driver would be sued for refusing to drive, this did not mean that payment for a completed journey was made wholly *ex gratia* (again, unless the arrangement was a contract for hire or reward, the MIB would not be liable to the injured person).²⁸

4. THE 'COMMERCIAL' CONTEXT: LEADING DECISIONS

- 6.12 *Non-binding commercial language.* Commercial agreements are presumed to be legally binding. Megaw J in *Edwards v. Skyways Ltd* (1964) expressed this as the starting point:²⁹

Where the subject matter of the agreement is some domestic or social relationship or transaction ... the law will often deny legal consequences to the agreement, because of the very nature of the subject matter. Where the subject matter of the agreement is not domestic or social, but is related to business affairs, the parties may, by using clear words, show that their intention is to make the transaction binding in honour only, and not in law; and the courts will give effect to the expressed intention.

- 6.13 But the two Court of Appeal decisions discussed in this paragraph (*Kleinwort Benson v. Malaysian Mining* (1989) and *Baird Textile Holdings Ltd v. Marks and Spencer plc* (2001)) show that the courts will not allow the commercial presumption of an 'intent to create legal relations' to run away with itself. There must be a clear promise, either an explicit one (which is not stated to be non-binding), or an implicit one which is clearly evidenced by the surrounding facts. Without this, the claim for breach of promise must founder. The 'commercial presumption' only kicks in if there is an express or apparent promise. The

²⁷ *The Times*, 4 December 1914 (on which see Scrutton LJ in the *Rose & Crompton* case, [1923] 2 KB 261, 288, CA).

²⁸ [1972] AC 301, 339–40, HL.

²⁹ [1964] 1 WLR 349, 354–5.

Court of Appeal's decision in *Kleinwort Benson v. Malaysian Mining* (1989)³⁰ shows that the presumption only arises if the courts can identify a promise, as opposed to a non-committal statement of current policy. The case concerned a so-called 'letter of comfort'.³¹ This is a quasi-guarantee by a parent company regarding its subsidiary's solvency and its general willingness to pay its subsidiary's debts. It is not a cast-iron guarantee. Indeed, the essence of a 'letter of comfort' is that it is less than an absolute guarantee. It will be unusual for the court to discover that, despite the label 'letter of comfort', the relevant agreement was intended to produce a binding contractual commitment. As Sir Anthony Clarke MR said in the Court of Appeal in *Associated British Ports v. Ferryways NV* (2009):³²

I regard a letter of comfort, properly so called, as one that does not give rise to contractual liability. The label used by the parties is not necessarily determinative. It is a matter of construction of the document as a whole ... [C]ontractual obligations may arise from a document when properly construed, even though, misleadingly, the label 'letter of comfort' has been applied to it ... Here the position remains that a document expressed to be a letter of comfort will usually not give rise to legal obligations (except, perhaps, as a warranty of present intention) but sometimes a primary continuing legal obligation may arise as a matter of construction, notwithstanding the rubric of a letter of comfort. As always, 'the court's task is to ascertain what common intentions should be ascribed to the parties from the terms of the documents and the surrounding circumstances' (*Kleinwort Benson* case, *per* Ralph Gibson LJ, at p. 789B).

The Court of Appeal's decision in *Baird Textile Holdings Ltd v. Marks and Spencer plc* (2001)³³ also shows that the 'commercial' presumption of enforceability cannot apply unless the court can first identify an 'explicit' or 'apparent' promise (the latter term concerning a clearly evidenced promise, even though not explicit; in other words, an 'apparent' promise is one which can be clearly inferred from conduct and context). These cases will be further examined in turn.

In Kleinwort Benson v. Malaysian Mining Corp. Bhd, the defendant, a parent company, had given the claimant lender the following written assurance: 'It is our policy to ensure that the business of [X, the subsidiary company] is at all times in a position to meet its liabilities to you under the [loan facility] arrangements.'³⁴ Duly comforted by the defendant's letter, the claimant lent a large sum to X, the subsidiary. X defaulted on repayment. It became insolvent amidst the cacophonous collapse of the world tin market. The lender sued the parent company upon the

30 [1989] 1 All ER 785, CA.

31 M. Furmston and G. J. Tolhurst, *Contract Formation: Law and Practice* (Oxford, 2010), chapter 7 ('letters of intent'; and including at 7.52 ff 'letters of comfort'); M. Furmston, 'Letters of Intent', in A. Burrows and E. Peel (eds.), *Contract Formation and Parties* (Oxford, 2010).

32 [2009] EWCA Civ 189; [2009] 1 Lloyd's Rep 595, at [24] to [27], *per* Sir Anthony Clarke MR.

33 [2001] EWCA Civ 274; [2002] 1 All ER (Comm) 737, at [59] to [70], *per* Mance LJ.

34 [1989] 1 All ER 785, CA.

letter of comfort. The Court of Appeal (reversing Hirst J) held that the comfort letter had no legal force.³⁵

The Court of Appeal's conclusion involved three steps.³⁶ First, the presumption that commercial promises are legally binding only applies if one can identify a promise. Secondly, the letter was couched in the present tense,³⁷ that is, that it *is* the parent company's policy to ensure that its subsidiary can meet its liabilities. That did not constitute a promise that it would continue to ensure that this was so.³⁸ On this point, Hirst J at first instance³⁹ had jumped the gun and applied the presumption without ascertaining whether there was indeed a clear promise here. Finally, there was evidence that, during their negotiations, the parent company had clearly refused to give the lender a standard guarantee. That could be taken into account when determining whether the comfort letter was intended to create a legal obligation (as an exception to the parol evidence rule, 14.26 ff; although a simpler approach is to say that the parol evidence rule does not apply at all if the relevant document is *prima facie* not a contract at all).

Next we turn to the *Baird* case in detail.

In *Baird Textile Holdings Ltd v. Marks and Spencer plc* (2001), the claimant had supplied goods to Marks and Spencer for over thirty years.⁴⁰ Marks and Spencer then 'dropped' that supplier. This was a commercial calamity because the claimant had only one customer, Marks and Spencer. Not surprisingly, the claimant sought compensation for breach of an alleged long-term supply agreement. However, there was no written or explicit long-term supply agreement. And so the supplier contended that such an undertaking could be inferred from these long-standing relations. The Court of Appeal held that no such long-term agreement could be inferred. In its view, the reason why the claimant could not point to a clear agreement was that Marks and Spencer, possessing greater economic power, had all along intended that matters should remain fluid.

The court rejected the claimant's attempt to shore up its fragile case by invoking the presumption that commercial arrangements are legally enforceable. Mance LJ noted that this would be to put the cart before the horse. Instead, the true logic of the analysis must be: (1) Do the facts disclose any real consensus between the parties that Marks and Spencer were committing themselves to making repeat orders, until they gave reasonable notice to

³⁵ *Ibid.*, at 797J.

³⁶ M. Furmston and G. J. Tolhurst, *Contract Formation: Law and Practice* (Oxford, 2010), 7.55, noting criticism by the New South Wales Commercial Division in *Banque Bruxelles Lambert v. Australian National Industries Ltd* (1989) 21 NSWLR 502, *per* Rogers J.

³⁷ M. Furmston and G. J. Tolhurst, *Contract Formation: Law and Practice* (Oxford, 2010), 7.56, noting that the New Zealand Court of Appeal did not adopt this point in *Bank of New Zealand v. Ginivan* [1991] 1 NZLR 178.

³⁸ [1989] 1 All ER 785, 794, CA (although acknowledging that this semantic point was not decisive: *ibid.*, at 794 and 796B).

³⁹ *Ibid.*, at 721.

⁴⁰ [2001] EWCA Civ 274; [2002] 1 All ER (Comm) 737, especially at [59] to [70], *per* Mance LJ.

terminate the chain of dealings? (2) If such an 'apparent' consensus emerges, there will be scope for the presumption in favour of legal relations to operate. This presumption would then be appropriate because this was clearly a commercial context. But the present claim foundered at stage (1): no clear implicit consensus could be found on these facts. Therefore, the *Edwards v. Skyways* (1964) (see 6.12 above) 'commercial' presumption of enforceability did not apply.

5. BORDERLINE OF 'COMMERCIAL AND NON-COMMERCIAL' RELATIONS

6.14 *Modahl v. British Athletic Federation Ltd* (2002)⁴¹ shows that there is an uncertain boundary between the 'commercial' and 'non-commercial' spheres of promise-making. The Court of Appeal decided that there can be a contract between a sportsman and his governing body, even if it has never been formally acknowledged (although no breach was shown). In these borderline cases, the courts cannot confidently invoke the presumption of enforceability, nor its converse. Instead, the court must make a value judgment. This can divide experienced judges (thus Jonathan Parker LJ dissented in the present case).

In 1994, Diane Modahl, a British international 800 metres runner, failed a laboratory test on a urine sample taken during an athletics meeting held in Portugal. This urine test result threatened to destroy her career. She protested her innocence. Eventually, in July 1995 the athletic authorities declared that the test had been a mistake. Apparently, the Portuguese experts were to blame for the error. However, in the meantime, Modahl had suffered turmoil. She sued the British Athletic Federation (BAF) for an alleged failure to deal fairly with her challenge to the accuracy of this urine test result. Her damages claim was for approximately £1m.

One of her contentions was that there was an implied contract, supported by consideration, between her and the BAF. If so, that contract would give her a right to claim damages for breach of the BAF's procedural rules. Modahl won on all the interesting points, but failed to show there had been a breach. The Court of Appeal decided the following points:

(1) Although there had been no exchange of offer and acceptance, there was a contract on these facts; it arose from repeated invitations to Modahl to run on behalf of the BAF.

(2) By a majority, there was an 'intent to create legal relations' on these facts;⁴² admittedly, this was not a fully fledged 'commercial relationship'; even so, the facts concerned an 'arm's length' relationship between a top-class sportswoman and her 'ruling bodies'. This context is a long way from the matrimonial relationship in *Balfour v. Balfour* (1919) (on which see 6.09).

41 [2001] EWCA Civ 1447; [2002] 1 WLR 1192, CA, at [50] to [54] and [105] (for earlier proceedings, see *Modahl v. British Athletic Federation Ltd* [1999] UKHL 37, partially striking out the claim).

42 [2001] EWCA Civ 1447; [2002] 1 WLR 1192, CA, at [51], [52] and [105], *per* Latham and Mance LJ (but Jonathan Parker LJ at [77] and [80] could discern no intent to create legal relations).

(3) Although the contract included an implied term that both parties would be governed by the BAF's rulebook, there had been no breach of that procedure on these facts; the court rejected her allegation that BAF's disciplinary process had been vitiated by bias; and Modahl's damages claim failed.

6. THE FUTURE

6.15 The status of 'intent to create legal relations' has become disputed. There are three views: (1) 'intent' should be allowed to oust the older doctrine of 'consideration' (see chapter 5 for that doctrine); (2) 'intent' is an unnecessary rider to ordinary principles of consensus; (3) 'intent' is here to stay, operating alongside 'consideration'. Of these three views, the third is correct.

6.16 *'Intent' destined to oust consideration?* This is the imperialistic view of the doctrine's prospects: that 'intent to create legal relations' will supplant the doctrine of consideration (see chapter 5 for that doctrine). According to this view, 'consideration' should be abolished (probably this might only be achieved by legislation; this doctrine is too deeply cemented as a feature of the common law to be simply abandoned by judicial decision). The present argument is that 'consideration' is an inexact and indirect way of posing the question addressed more precisely by the doctrine of 'intent to create legal relations': is this promise supported by a shared wish to create legally binding rights and duties, or is the promise too casual and informal to have legal force? However, this 'imperialistic' view is open to objection. For example, McKendrick rightly doubts whether the 'intent' doctrine will or should oust 'consideration':⁴³ at the core of 'consideration' is the legal system's refusal to give effect to gratuitous promises unless they are (as it were) solemnised in a formal way (by use of a 'deed', 5.03). The better view is that this bargain test is not just a roundabout way of discerning an 'intent' to create legal rights (on the basis of a rule-of-thumb inference that a 'bargain' is normally intended to be legally binding, but a promise of pure generosity is not). 'Consideration' encapsulates a paternalistic policy: that the promisor (and those interested in his solvency and prosperity) should be protected against the risk of squandering too liberally his assets (and energies) by making gratuitous promises. And so X's promise to give £1m to Y, or to release T from his debt of £5m, will be given effect only if X makes the effort to clothe his benevolence in the form of a deed (see 5.03 for the requirements of a deed). It is not enough that X in these situations utters the incantation 'this promise is accompanied by an intention to create legal relations'. Even if the promise were sincerely intended to create legal rights, the purpose of the 'consideration' doctrine is to give the gratuitous promisor the right to change his mind. And so he cannot be sued for the sum not paid nor (in the case of releases) can he, as creditor, be prevented from suing X for the balance not in fact paid (this last point is the common law starting point; but equity, taking the form of promissory estoppel, has qualified the position; see 5.54).

43 E. McKendrick, *Contract Law* (8th edn, London, 2009), 5.29.

- 6.17 *'Intent' doctrine should be subsumed by 'offer and acceptance'*. Secondly, there is a bold and sceptical view: that intent to create legal relations should be excised as a separate doctrine. Instead, 'intent' should be treated as merely an aspect of the 'offer and acceptance' bundle of rules.⁴⁴ However, in response to this, it should be noted that the independent nature of the intention to create legal relations doctrine is widely accepted. The doctrine enjoys a secure place both in the practice of the courts and in leading textbooks.
- 6.18 *Orthodoxy*. The third and orthodox approach is that the doctrine of intent to create legal relations has long since taken firm root as an independent doctrine. Failure to satisfy this requirement will preclude legal enforcement. It is thus a separate test, operating additionally to the bargain test of 'consideration'⁴⁵ and the requirement of certainty. Thus, Mance LJ said in the *Baird* case (2001):⁴⁶ 'For a contract to come into existence, there must be both (a) an agreement on essentials with sufficient certainty to be enforceable and (b) an intention to create legal relations.' Element (a) is arguably an elision of 'offer and acceptance' (see chapter 3) and 'certainty' (see chapter 4); element (b) has been the subject of the present chapter; and the learned judge clearly did not intend to doubt the general requirement of 'consideration' (the subject of chapter 5).

44 *Butterworths Law of Contract* (3rd edn, London, 2007), 2.169; J. O'Sullivan and J. Hilliard, *The Law of Contract* (4th edn, Oxford, 2010), 3.12, suggest that 'the doctrine of intent to create legal relations is better viewed as part of the rules on offer and acceptance'. For a rejoinder, see E. McKendrick, *Contract Law: Text, Cases and Materials* (4th edn, Oxford, 2010), 291–3.

45 McKendrick, *ibid.*, noting that, in Australia, the 'doctrine' has been downgraded to an issue of the burden of proof.

46 [2001] EWCA Civ 274; [2002] 1 All ER (Comm) 737, at [59].

IV

Third parties and assignment

Chapter contents

1. Introduction *para. 7.01*
2. The common law doctrine of privity *para. 7.03*
3. Joint promisees at common law *para. 7.10*
4. 'Trusts of promises': a direct right of action *para. 7.12*
5. Actions brought by the promisee *para. 7.19*
6. The Contracts (Rights of Third Parties) Act 1999 *para. 7.34*
7. The benefit of exclusion clauses at common law and under the 1999 Act *para. 7.59*
8. Privity of contract and 'burdens' *para. 7.67*

7

Third parties

1. INTRODUCTION¹

7.01 Summary of main points

- (1) At common law (that is, under the judicial law established prior to the change introduced by the Contracts (Rights of Third Parties) Act 1999) (see the summary at (3) below), a third party cannot enforce a contract intended by the parties to be for her benefit. And so at common law, a non-party, T, cannot sue A directly if A promises B that A will pay £1,000 to T, in return for a counter-promise by B to do something. It is different if B assigns this debt to Z, because Z can then sue A. But assignment can only occur after the formation of the contract between A and B. Assignment is examined in chapter 8.
- (2) The Law Commission successfully recommended a legislative system of third party rights:² the Contracts (Rights of Third Parties) Act 1999.
- (3) The 1999 Act enables a third party to acquire a direct right of action (or the right to benefit from an exclusion clause) either by explicit language (A and B state clearly that 'T can sue A directly') or by implication (A and B agree that A will 'confer a benefit' on T, for example, that A will pay a sum to T); this will normally entitle T to sue A for this amount, even though the right of action was not spelt out; but A might succeed in countering this inference.
- (4) Despite the revolution of the 1999 Act, the common law remains relevant, for several reasons:

1 R. Merkin (ed.), *Privity of Contract* (London, 2000); for theoretical discussion, see P. Kincaid (ed.), *Privity* (Aldershot, 2001); V. V. Palmer, *The Paths to Privity* (San Francisco, 1992), examines the history of this doctrine; for a review of this book, N. Andrews, (1995) 69 *Tulane Law Review* 1393; for comparative discussion, see V. V. Palmer, 'Contracts in Favour of Third Persons in Europe' (2003) 11 *European Review of Private Law* 8–27; and, on the major English statute, see the literature cited in note 87 below.

2 Law Commission, *Privity of Contract: Contracts for the Benefit of Third Parties* (Law Commission Report No. 242, Cm 3329, London, 1996).

- (a) To the extent that the Act governs current contracts, the statute overrides the perceived objections to the 'third party contractual rights at common law' rule; and an understanding of that background is therefore required.
 - (b) Some types of contract are excluded from the legislative scheme; to that extent, the common law rule continues to bar a third party from suing.
 - (c) It remains possible at common law for A to promise to benefit B1 and B2 jointly. This is the doctrine of 'joint promisees': B1 provides consideration jointly on behalf of B1 and B2; A's promise is made to these jointly; B1 and B2 must sue A jointly, but if either B1 or B2 dies, the right of action against A devolves entirely upon the survivor.
 - (d) The promisee's capacity to obtain remedies in respect of A's breach remains governed by common law principles. B's capacity to sue A in respect of non-performance is of great practical importance (see point (7) below).
- (5) The greatest challenge to the common law privity rule (summarised at (1) above) was equity's invention in the eighteenth century of 'trusts of promises'. The benefit of A's promise to pay money or to transfer property to T (known as a 'chose in action') can be held by B on trust for T, B thereupon becoming obliged in equity to sue A for T's benefit. But, if B fails to sue A, T (as the 'beneficiary' of the trust) can take the initiative and sue A for default in performance (a plain reversal by equity of the common law privity doctrine). However, the Court of Appeal in *Re Schebsman* (1944)³ held that the courts would no longer benevolently imply such a trust. This was a 'tipping point'. After 1944, a trust of a promise had to be based on explicit language indicating the contracting parties' shared intention to confer on T an irrevocable entitlement to the benefit of A's promised performance.
- (6) The House of Lords in *Midland Silicones v. Scruttons* (1962)⁴ held that a third party, Z, cannot take the benefit of an exclusion clause (a 'shield' against an action by X) even though parties X and Y have clearly intended that Z should so benefit. This has proved to be an irksome extension of the common law privity doctrine. But the *New Zealand Shipping* case (1975)⁵ enabled commercial lawyers to circumvent the rule in the *Scruttons* case by finding an express contract between X and Z, the only content of which is that Z performs work in return for X's promise of an exclusion clause; X and Z are then in privity of contract; in this way, the *Scruttons* rule had been sidestepped. Happily, this common law contortion is no longer necessary because the Contracts (Rights of Third Parties) Act 1999 enables a third party to acquire the benefit of an exclusion clause.

3 [1944] Ch 83, CA.

4 [1962] AC 446, 473, HL.

5 [1975] AC 154, PC.

- (7) As mentioned at (4)(d), even after the 1999 Act, it remains important to consider the capacity of the promisee to sue in respect of A's breach of contract, even though the 'target' of A's promise is A and B's agreement that A should benefit T, the third party.
- (a) However, B cannot sue A in *debt* if A's promise was to pay money to T.
 - (b) Furthermore, B cannot sue A for *damages* unless B has suffered *personal* loss (the so-called rule in *Woodar v. Wimpey* (1980), though in fact this rule antedates that case) (7.23). Exceptions to the rule in *Woodar v. Wimpey* have been introduced, notably in the context (governed by decisions culminating in the *Panatown* case (2001)) where A's promise to B was to build on T's land, or carry out repairs to buildings on that land (whether T at all relevant points owned this site or T acquired it subsequent to the formation of A and B's contract).
 - (c) If neither a claim in *debt* or for *damages* offers substantial protection of B's interest in A's performance, exceptionally B can obtain an order for *specific performance* (an equitable remedy), and thus compel A to execute his promise for T's benefit (on pain of contempt of court if A defaults), as illustrated by *Beswick v. Beswick* (1968).

SELECTED FURTHER READING

On damages at the suit of the promisee

A. Burrows, 'No Damages for a Third Party's Loss' (2001) 1 *Oxford University Commonwealth Law Journal* 107

On the 1999 Act

Law Commission, *Privity of Contract: Contracts for the Benefit of Third Parties* (Law Commission Report No. 242, 1996), notably Parts VII–XI

A. S. Burrows, 'The Contracts (Rights of Third Parties) Act 1999 and its Implications for Commercial Contracts' [2000] *Lloyd's Maritime and Commercial Law Quarterly* 540–54

N. Andrews, 'Strangers to Justice No Longer: Reversal of the Privity Rule under the Contracts (Rights of Third Parties) Act 1999' [2001] *CLJ* 353–81

R. Stevens, 'The Contracts (Rights of Third Parties) Act 1999' (2004) 120 *LQR* 292–323 (who bemoans its enactment)

7.02 Summary of 'the no third party burden' principle

- (8) Another aspect of the 'privity' concept is that a third party cannot be placed under a contractual obligation if he has not consented freely to it: contracting parties

X and Y cannot thrust a duty on Z, a non-party, to act for their benefit or to pay money, etc. This 'no third party burden' principle seems plainly just (see 7.67 for discussion).

- (9) But there are different types of 'burden'. To impose a positive duty on a non-party to pay money or physically act is clearly intolerable. But to impose a restriction on a third party's freedom or enjoyment of his usual rights is less burdensome. The concept of property rights binding on the world at large and the notion of a non-party's 'implied consent' to certain restrictions have been used to introduce the following qualifications to the 'no third party burden' principle. Four points will be made here:
- (a) Z must not interfere consciously with X and Y's contractual rights. Z will become liable *in the law of tort* if he either induces a breach by X or Y of the contract between X and Y, or if Z interferes using unlawful means with the performance of the same contract.
 - (b) A purchaser of land (Whiteacre) can become 'subject to' a restrictive covenant affecting that land. The covenant, to which the purchaser is often a third party, is regarded as binding Whiteacre and benefiting another piece of land, Greenacre.
 - (c) In the context of goods, Z can also find that his ownership is qualified by a contract between X and Y concerning those goods (see the *Swiss Bank* case at 7.73 below). This is not unjust provided two conditions are satisfied: first, that Z was aware of this restriction and, secondly, that the effect is not to impose a positive obligation upon Z.
 - (d) Similar conditions underpin the doctrine of 'bailment on terms'. Here, Z becomes subject to restrictions – either an exclusion clause or an exclusive jurisdiction clause – contained in a sub-bailment of Z's goods by X to Y, provided Z has at least implicitly consented to the sub-bailment (for the definition of bailment, see 7.75 below).

2. THE COMMON LAW DOCTRINE OF PRIVACY

- 7.03 At common law, A and B cannot confer on T, a third party, a direct right of action against A (for the possibility that, after the contract's formation, B might assign his right to X, 'the assignee', see chapter 8). Nor can parties A and B give T, a third party, the benefit of a 'shield', notably an exclusion clause (generally on exclusion clauses, see chapter 15). Such a clause might benefit T if A were to sue him in the tort of negligence. Furthermore, freedom of contract (1.08) demands that X and Y cannot impose a burden on a third party, Z, 'behind his back', that is, without Z's consent. And so Z, a third party, cannot be subjected to a duty to pay money to X or Y, nor can X and Y impose on Z the burden of an exclusion clause, preventing Z from being able to sue X or Y, or restricting his capacity to obtain compensation (unless an exceptional context can be found, 7.76).

- 7.04 *The turning point at common law.* The cases were in a confused state⁶ before *Tweddle v. Atkinson* (1861).⁷ The court in that case held that the third party could not sue for breach of promise because he had not provided consideration for the promise, that is, he had not bought the right to sue.

Tweddle v. Atkinson (1861) concerned a written post-nuptial agreement between Tweddle senior (the father of Tweddle junior) and Guy (the father-in-law of Tweddle junior). Tweddle junior was therefore a third party to the contract between Tweddle senior and Guy, who promised each other that they would pay, respectively, £100 and £200 to Tweddle junior, the third party, before 21 August 1855. Guy, the father-in-law, failed to pay and died. Tweddle senior, still alive, had also failed to pay. The son, showing filial respect, sued only Guy's executor for £200. But the claim failed. The court held that the son, as a third party, had not provided consideration for the promise, that is, he had not bought the right to sue.

This was a strong denial of a third party right of action because the parties had expressly stipulated that T, the son, should be able to sue in equity or at common law. In light of this last fact, it is odd that the son had not instead chosen to sue in the Court of Chancery (which had yet to merge with the common law courts; for which see the Judicature Acts 1873 and 1875; and on the concept of a 'trust of a promise', see 7.12). The son could then have sued in his own name, joining the father-in-law's estate and his own father as co-defendants, but only the father-in-law being liable to pay.

- 7.05 The next major common law decision is *Dunlop Pneumatic Tyre Co. Ltd v. Selfridge & Co. Ltd* (1915).

Dews had agreed with Dunlop that Dews would not sell Dunlop tyres below a certain price and, further, that retailers buying tyres from Dews would be required to give the same undertaking. Selfridge bought tyres from Dews and gave the undertaking just mentioned. But Selfridge then sold the tyres below the minimum price. Dunlop sued Selfridge for this alleged breach. His claim failed.

The decision contains two grounds for denying a claim by the third party. First, Lord Haldane LC endorsed the 'consideration' requirement established in the *Tweddle* case (1861). In the *Dunlop* case (1915), Lord Haldane LC said:⁸

6 V. V. Palmer, *The Paths to Privity* (San Francisco, 1992), examines the history of this doctrine; for a review of this book, N. Andrews, (1995) 69 *Tulane Law Review* 1393.

7 (1861) 1 B & S 393; 30 LJQB 265; 4 LT 468; cf *Lawrence v. Fox*, 20 NY 268 (1859) (the New York Court of Appeals, two years before the *Tweddle* case, decided that a third party beneficiary did have a right of action).

8 [1915] AC 847, 853, HL.

[I]f a person with whom a contract not under seal has been made is to be able to enforce it consideration must have been given by him to the promisor or to some other person at the promisor's request.

But Lord Haldane LC made an additional point, on which the *Tweddle* case had been silent: that the third party could not sue because he was not an addressee of the promise made by A to B. In other words, *the third party was not a promisee*. Therefore, A was committing himself only to an obligation towards B but not to an obligation towards the third party.⁹

[C]ertain principles are fundamental. One is that only a person who is a party to a contract can sue on it. Our law knows nothing of a *jus quaesitum tertio* [a direct right of action by the third party] arising by way of contract. Such a right may be conferred by way of property, as, for example, under a trust, but it cannot be conferred on a stranger to a contract as a right to enforce the contract *in personam* [as a personal obligation].

As Treitel observes, the 'new point', made by Lord Haldane, that 'only a party can sue on a contract', is merely a restatement of the privity doctrine, rather than an independent and satisfactory reason for adopting that doctrine.¹⁰

7.06 In various twentieth-century cases, Lord Denning tried unsuccessfully to subvert the common law privity doctrine, using a number of arguments and devices, as the author has examined in detail elsewhere.¹¹ His 'Waterloo' in this campaign was the House of Lords' reversal of his (more precisely, the Court of Appeal's) decision in *Beswick v. Beswick* (1968) (7.22).¹²

7.07 *Assessment of the common law rule.* Therefore, the two main suggested justifications (for a third argument, 7.08) for the common law rule are:

- (1) that T has not provided consideration for A's promise; T is a 'donee beneficiary' or a 'volunteer'; T has not 'bought the right to sue'; this is the *ratio* in *Tweddle v. Atkinson* (1861) (7.04);¹³
- (2) that the third party T is not 'privity to the contract'; this is the *ratio* in the *Dunlop* case (1915) (7.05).

As for (1), it can be objected that it should not matter that only B has provided consideration. The function of consideration is to render the contract binding as between A and B

⁹ *Ibid.*

¹⁰ The 'only a party can sue' argument 'begs the question': *Treitel* (12th edn, London, 2007), 14-017.

¹¹ N. Andrews, (1995) 69 *Tulane Law Review* 1393.

¹² [1968] AC 58, HL (overturning [1966] Ch 538, CA); in the Court of Appeal, Lord Denning MR, with Danckwerts LJ's support, invoked section 56 of the Law of Property Act 1925 to undermine the common law authorities; on this difficult provision, see Neuberger J in *Amsprop Trading Ltd v. Harris Distribution Ltd* [1997] 1 WLR 1025, 1032, and *Treitel* (12th edn, London, 2007), 14-136 to 14-138.

¹³ (1861) 1 B & S 393; 30 LJQB 265; 4 LT 468.

(in the absence of a ‘deed’, for which see 5.03). It is an unconvincing extension of the role of consideration to require a third party to have earned or bought the right to sue given him by the contracting parties. A second weakness of the consideration argument is that, one second in time after the contract’s formation, B can assign the benefit of the contract to X, an assignee. The fact that X has not given anything to earn this right does not preclude him from acquiring a right by assignment. Thus, if A promises to pay B £1,000, B can assign (make a present of) this debt, a chose in action, to T; T will then have a direct right of action against A; T need not provide consideration to be able to take advantage of the assignment (generally on assignment, see chapter 8). Frustrated by English law’s misguided decision to invoke the doctrine of consideration to deny a third party a right of action, Lord Dunedin (a Scottish law lord) said in the *Dunlop* case (1915):¹⁴

My Lords, I confess that this case is to my mind apt to nip any budding affection which one might have had for the doctrine of consideration. For the effect of that doctrine in the present case is to make it possible for a person to snap his finger at a bargain deliberately made, a bargain not in itself unfair, and which the person seeking to enforce it has a legitimate interest to enforce.

As for argument (2), the requirement of ‘pure privity’, this rests on a dogma and is conspicuously circular: a third party cannot sue on a contract; this is because only a party can do so; and a third party is not a party! As the Law Commission suggested when recommending reform (7.34), there is no convincing reason why the contracting parties should be denied the capacity to vest a direct right in a third party, even if A’s promise to do so is addressed solely to B and even though T, the target of the intended performance, is not a co-promisee.¹⁵

- 7.08 A third reason why it had been considered dangerous for T to gain a direct right of action is because such a right would be ‘irrevocable’, that is, it could not be altered or extinguished by A unilaterally, nor even consensually by A and B. This reluctance to fetter A and B’s powers of ‘revocation’ or ‘variation’ is evident in *Re Schebsman* (1944),¹⁶ the leading modern decision concerning the test for finding a ‘trust of a promise’ in favour of a third party (7.15). More generally, as the Law Commission rightly noted, the present argument links directly with the fact that the third party’s right arises gratuitously, without his providing any consideration for it.¹⁷ He should not have initial ‘sovereignty’ over A and B’s agreement, although the position might change once he has acted on it, or assented to it. For this reason, we shall see that the Contracts (Rights of Third Parties) Act 1999 contains various rules on this topic (7.48). In essence, under the 1999 Act A and B can vary or extinguish their contract until (1) T notifies A that he accepts the contract or

¹⁴ [1915] AC 847, 855, HL.

¹⁵ Law Commission, *Privity of Contract: Contracts for the Benefit of Third Parties* (Law Commission Report No. 242, Cm 3329, London, 1996), 6.13 ff.

¹⁶ [1944] Ch 83, CA.

¹⁷ Law Commission, *Privity of Contract: Contracts for the Benefit of Third Parties* (Law Commission Report No. 242, Cm 3329, London, 1996), 6.15.

(2) T has relied on the contract. These ‘cut-off’ points provide a balancing of the interests of the three members of the third party triangle.

- 7.09 *Extension of the privity doctrine to deny third parties the protection of exclusion clauses.* In the *Scruttons* case (1962)¹⁸ (7.59), the House of Lords held that a non-party T cannot ‘take advantage’ of a contract, even passively, as a ‘shield’ against A’s action, even though A and B have explicitly agreed that A cannot sue T in tort (or that T’s liability is restricted). This decision was commercially unattractive because it required greater insurance expenditure, to the ultimate detriment of users of the relevant services (7.61). As we shall see, this problem can now be circumvented at common law (7.63) and is directly countered by the 1999 Act (7.62).

3. JOINT PROMISEES AT COMMON LAW

- 7.10 At common law, A can direct his promise at more than one person and render them joint promisees. It follows that neither is a third party. Consideration to support A’s promise can be validly supplied jointly by B1 and B2, or even *de facto* by one, provided in this last situation the consideration is given ‘jointly on behalf of B1 and B2’. The latter proposition is supported by Australian *dicta* in *Coulls v. Bagot’s Executor & Trustee Co. Ltd* (1967)¹⁹ and by many English commentators.²⁰

However, Coote, a New Zealand commentator, suggests that B2 should only be treated as having provided consideration if B2 could be sued for its non-provision in the event of B1’s failure to provide it.²¹ It is submitted that Coote’s more restrictive approach is unattractive. It should be enough that B1 has in fact provided consideration jointly on B1 and B2’s behalf. The law can then deftly enable B2 to overcome the objection that he has in reality not ‘bought the right to sue A’ (for the ‘consideration problem’ where the claimant is a third party, rather than a joint promisee, see the discussion at 7.04 and 7.07 of the rule in *Tweddle v. Atkinson* (1861)).²²

- 7.11 A further common law rule is that a joint promisee can only sue *if he joins his fellow promisee in the relevant claim*.²³ Rule 19.3 of the Civil Procedure Rules 1998 provides:

Where a claimant claims a remedy to which some other person is jointly entitled with him, all persons jointly entitled to the remedy must be parties unless the court orders otherwise.

¹⁸ [1962] AC 446, 473, HL.

¹⁹ (1967) 119 CLR 460, 478; (1967) 40 ALJR 471, 483 (High Court of Australia), *per* Windeyer J (on the facts, the majority held that there had been no joint promise).

²⁰ E.g. Sir Jack Beatson in Law Commission Consultation Paper, *Privity of Contract: Contracts for the Benefit of Third Parties* (Law Commission Consultation Paper No. 121, London, 1991), at 3.33; *Chitty on Contracts* (30th edn, London, 2008), 3-042; *Treitel* (12th edn, London, 2007), 13-032.

²¹ B. Coote, ‘Consideration and the Joint Promisee’ [1978] CLJ 301, 304–5.

²² (1861) 1 B & S 393; 30 LJQB 265; 4 LT 468.

²³ *Treitel* (12th edn, London, 2007), 13-021; *Chitty on Contracts* (30th edn, London, 2008), 17-09 and 17-010.

The dual purpose of this 'joinder rule' is to protect the promisor against the risk of successive actions and to ensure that the court can receive all relevant arguments and information. However, once a joint promisee dies, the doctrine of 'survivorship' causes his right of action to pass to the surviving promisee, rather than to the deceased's estate. If, for example, A promised in 2010 to pay £1,000 to B1 and B2, and B1 died in 2011, thereafter B2 alone can sue A.

4. 'TRUSTS OF PROMISES': A DIRECT RIGHT OF ACTION

7.12 *Genesis*. The 'trust of promises' is the concept that B, as promisee, can assume a second role and become trustee of A's promise to benefit T. The benefit of A's promise to pay money to T, or to transfer property to T (such promises are known as 'choses in action'), can be held by B on trust for T, B thereupon becoming obliged in equity to sue A for T's benefit. This is based on the notion that the *promise to pay money or to transfer property* is itself a valuable asset, an intangible 'chose in action', even though it is merely a personal relation, a right *in personam*. This equitable concept provided a means of side-stepping the common law rule against contractual claims by third parties.²⁴ This type of trust originated in Lord Hardwicke LC's decision in *Tomlinson v. Gill* (1756).²⁵ This device operated attractively for nearly two centuries. But the Court of Appeal's decision in *Re Schebsman* (1944)²⁶ (7.15) almost killed it off by insisting that a trust of a promise requires express language. Thereafter, no longer would the courts *imply* such a trust in order to circumvent the common law privity doctrine.

7.13 *Who declares the trust?* In the usual case, B will have provided consideration. Then it will be B who declares the trust of a promise, or A and B might jointly agree to its creation. But, if (unusually) A's promise is gratuitous, resting on a deed (5.03), Feltham has suggested that it will be A alone who can create the trust and so appoint B to be trustee.²⁷

7.14 *Effects of trusts of promises*. The effects of a 'trust of promises' are:

- (1) B can sue A on T's behalf; indeed, B is obliged by equity to sue A on T's behalf.
- (2) If B fails to sue A, T can sue A (joining B as co-defendant); this is the elusive *ius quaesitum tertio* (the direct right of action by the third party) which was denied at common law under *Tweddle v. Atkinson* (1861)²⁸ and the *Dunlop* case (1915)²⁹ (7.04 and 7.05).³⁰

24 *Fletcher v. Fletcher* (1844) 4 Hare 67 (Wigram V-C); *Lloyd's v. Harper* (1880) 16 Ch D 290, CA; *Les Affréteurs Réunis SA v. Leopold Walford (London) Ltd* [1919] AC 801, HL; A. L. Corbin, (1930) 46 LQR 12; J. Jaconelli, [1998] Conv 99; M. MacIntyre, (1965) 2 *University of British Columbia Law Review* 103; Lord Wright, (1939) 55 LQR 189, 208; R. Merkin (ed.), *Privity of Contract* (London, 2000), 2.18 to 2.25; J. Langbein, (1997) 105 *Yale Law Journal* 625, 646–7.

25 (1756) Ambler 330; V. V. Palmer, *The Paths to Privity* (San Francisco, 1992), 130–4.

26 [1944] Ch 83, CA.

27 J. D. Feltham, (1982) 98 LQR 17, approving the approach taken in the USA.

28 (1861) 1 B & S 393; 30 LJQB 265; 4 LT 468.

29 [1915] AC 847, HL.

30 Affirmed by a *dictum* of Lord Wright in *Vandepitte v. Preferred Accident Insurance Corporation of New York* [1933] AC 70, PC; Colman J overlooked this point in *Nisshin Shipping Co. Ltd v. Cleaves & Co.*

- (3) The claim based on a trust of a promise is not in respect of A's breach towards B, but instead concerns A's direct obligation to T.³¹ Accordingly, damages (intended for T's benefit), the agreed sum (payable to T) or property (intended to be transferred to T), will be held by B on trust for T.³²
- (4) A, B and T should each be party to the litigation (or arbitration reference); however, this 'joinder requirement' is intended to protect A against potential double suit by B and T in successive litigation;³³ and so A can 'waive' the need to join B, as the House of Lords acknowledged in *Walford's Case* (1919);³⁴ if such a waiver occurs, the action will only involve T and A, and B will have dropped out of the picture.
- (5) The fact that B assumes a *trust obligation* to protect T's interests means that B cannot agree, or otherwise act, to reduce or extinguish T's rights against A.

7.15 *Test.* Since *Re Schebsman* (1944),³⁵ there have been two requirements for the creation of a trust of a promise: first, the contracting parties must use express language to create the trust, for example, 'this promise is to be held on trust for T' or 'B is to hold A's promise for T's benefit'; secondly, A and B must clearly intend that T should acquire irrevocable rights against A,³⁶ although this adds little to the notion of an express wish to create a trust.

7.16 It is unfortunate that *Re Schebsman* (1944) ended the courts' use of implied trusts of a promise.³⁷ Pre-*Schebsman* case law had not insisted on strict proof of an intention to create a trust of a promise (for example, *Fletcher v. Fletcher* (1844), where Wigram V-C had held that a promise by A to B to pay a large sum to T imported a trust of a promise in favour of T, without the need for an explicit declaration of a trust).³⁸ This liberal line of cases had been supported by Corbin at the Yale Law School.³⁹ Nevertheless, the Court of Appeal in *Re Schebsman* (1944) turned its back on this line of cases.⁴⁰

7.17 However, some 'fossilised relics' from the pre-*Schebsman* era of implied trusts survive. These might be rationalised as based on *mercantile custom*. For example, in *Walford's*

Ltd [2003] EWHC 2602 (Comm); [2004] 1 All ER (Comm) 481; [2004] 1 Lloyd's Rep 38 (see 7.58 on this case).

31 *Lloyd's v. Harper* (1880) 16 Ch D 290, CA.

32 *Ibid.*

33 Cf potential double liability and joinder, *Carr-Glynn v. Frearson* [1998] 4 All ER 225, 235–6, CA, *per* Chadwick LJ, in the context of *tortious* claims for defective will-making and related testamentary services.

34 *Les Affréteurs Réunis SA v. Leopold Walford (London) Ltd* [1919] AC 801, HL.

35 [1944] Ch 83, CA.

36 *Vandepitte v. Preferred Accident Insurance Corporation of New York* [1933] AC 70, 80, PC.

37 [1944] Ch 83, CA.

38 (1844) Hare 67, Wigram V-C.

39 A. L. Corbin, (1930) 46 LQR 12; G. H. Treitel, *Some Landmarks of Twentieth Century Contract Law* (Oxford, 2002), 51, notes that Corbin had been asked to write this article by Goodhart, editor of the *Law Quarterly Review*; on Corbin's 1951 treatise, chapter 46, see Treitel, *ibid.*, at 52.

40 Corbin's article, *ibid.*, was cited by the first instance judge ([1943] Ch 366, 370) and so was visible to the Court of Appeal.

Case (1919), the House of Lords gave effect to an implied trust of a promise within a clause between a ship-owner, A, and a charterer, B, for the payment by A of commission to T, a shipbroker, in recognition of fixing the charterparty (a contract for the hire of a ship). That clause was inserted into the contract by B in favour of T.⁴¹ The House of Lords decision that an implied trust of a promise arose in favour of T meant that B was obliged to sue A on T's behalf, failing which T could sue A directly. *Walford's Case* (1919) was followed by Colman J in *Nisshin Shipping Co. Ltd v. Cleaves & Co. Ltd* (2004) (for more on this case, see 7.41 and 7.58).⁴²

7.18 *Differences between trusts of promises and direct rights of action under the 1999 Act.* As explained at 7.34, the Contracts (Rights of Third Parties) Act 1999 creates a direct right of action exercisable by T against A, and section 7(1) of the Act preserves any parallel direct rights of action which T might have. Sometimes, T will have both a third party action under the Act and a trust of a promise. If so, various differences arise between these two claims:⁴³

- (1) Trusts of promises are irrevocable: under a trust of a promise, T acquires at the date of formation an irrevocable right; A and B cannot vary or extinguish it without T's consent. But, under the Act, A and B can agree to vary or extinguish A's rights without his consent until T has notified A or relied on A's promise.
- (2) Trusts of promises are confined to money and property transfers: a trust of a promise is applicable only to promises to pay money to T or transfer property to T (and not, for example, a contract to perform services for T's benefit, nor a contract to confer on T the benefit of an exclusion clause).⁴⁴ But the Act covers *all* species of contractual obligation in favour of T and the conferring of the protection of exclusion clauses upon T.
- (3) Trusts of promises require explicit creation: a trust of a promise can only be created by express language (7.15), whereas rights under the Act under 'limb 2' (7.41) can arise as an offshoot of an intent to confer a benefit on T (without the parties' express stipulation that T shall have a direct right of action).
- (4) Trusts-of-promises litigation normally requires all three parties to participate: in litigation involving a trust of a promise, all three parties must be joined as parties (7.14), unless A 'waives' this requirement (7.14 at (4) above). Under the Act, T can sue A without joining B as a party, whether in arbitration or in litigation.
- (5) As for arbitration (7.58), section 8(1) of the Act enables T to accede to A and B's arbitration agreement, if T is suing A under section 1 of the Act (7.39). However,

41 *Les Affréteurs Réunis SA v. Leopold Walford (London) Ltd* [1919] AC 801, HL (applying *Robertson v. Wait* (1853) 8 Ex 299); and *UDT v. Kirkwood* [1966] 2 QB 431, 454–5, CA.

42 [2004] EWHC 2602 (Comm); [2004] 1 All ER (Comm) 481; [2004] 1 Lloyd's Rep 38.

43 *Treitel* (12th edn, London, 2007), 14-096; N. Andrews, 'Strangers to Justice No Longer: Reversal of the Privity Rule under the Contracts (Rights of Third Parties) Act 1999' [2001] CLJ 353, 377–8.

44 On this point, see *Southern Water v. Carey* [1985] 2 All ER 1077, 1083G, *per* Judge David Smout QC, Official Referee.

section 8(1) does not ‘unlock the door to A and B’s arbitration agreement’ if T’s claim is made under a trust of a promise; instead, T can bring a trust claim only by court proceedings.

5. ACTIONS BROUGHT BY THE PROMISEE

7.19 Although the Contracts (Rights of Third Parties) Act 1999 will often give T a direct claim against A, this statute does not eliminate the possibility of B suing A at common law. And so, *in exercise of his common law rights as promisee*, B can sue A for breach of contract, even though the main aim of A’s promise was to benefit T. We will examine B’s access to the following remedies: debt (not available if the promise were to pay the sum to T), specific performance (exceptionally available to B), damages (a problematic topic) and declarations. As for damages, the Act contains a provision designed to counter the risk of A being doubly liable for the same loss (7.54).⁴⁵

7.20 *Debt*. If A promises B, for consideration, to pay a fixed sum to C, B cannot sue and obtain this sum (even on T’s behalf). The twofold explanation for this is: first, A promised to pay T and not to pay B (it would be different if B had mandated A to pay T, but B had retained the power to *nominate another payee, including himself*);⁴⁶ secondly, even if B were to recover the debt on T’s behalf, common law lacks the machinery to ensure that B would not keep the money. B would then be unjustly enriched at T’s expense. It is regrettable that the law lacks the flexibility to overcome both these points. The two points *might have* been overcome by permitting B to sue A for debt on condition that *B should be required to hand the money to T*.⁴⁷ However, there are two ways round this problem: (1) if A promises to pay B, B can immediately assign that debt claim to T and T as assignee can sue A directly (on assignment, see chapter 8); or (2) under the 1999 Act, T might now have a direct claim against A for payment (7.34).

7.21 *Specific performance*. This equitable remedy (18.13) is an order that the promisor must do exactly what he promised to do, such as convey or purchase land, or transfer shares in a private company. The promisor is compelled to perform on pain of punishment for contempt of court (18.13). An important restriction is that specific performance is only available if other remedies are inadequate on the relevant facts (18.14). Another restriction is that equity will not compel a person to perform an obligation for the provision of personal services, such as singing or acting in a play (18.17).

⁴⁵ Law Commission, *Privity of Contract: Contracts for the Benefit of Third Parties* (Law Commission Report No. 242, Cm 3329, London, 1996), 5.12 to 5.17.

⁴⁶ *Beswick v. Beswick* [1968] AC 58, 72, 96, HL, *per* Lords Reid and Upjohn (cf the different result in *Cleaver v. Mutual Reserve Fund Life Association* [1892] 1 QB 147, probably turning on the relevant statute, *ibid.*, at 157).

⁴⁷ N. Andrews, ‘Does a Third Party Beneficiary Have a Right in English Law?’ (1988) LS 14, 29, for criticism; similarly, A. S. Burrows, *Remedies for Torts and Breach of Contract* (3rd edn, Oxford, 2004), 434–5.

7.22 In the present third party context, the leading case concerning specific performance at the suit of B, the promisee, is *Beswick v. Beswick* (1968).⁴⁸ In this case, B transferred his coal-merchant's business to A, his nephew, and A promised B to pay £5 per week to T (for the rest of T's life). T was B's wife and A's aunt. After B's death, A paid £5 to T, the widow, and then refused to pay more. T was both a third party *and the promisee's widow and administrator of B's estate*. In this (fortuitous) second capacity, B (the administrator) obtained an order of specific performance to compel A to honour the obligation to make these periodical payments to T. The House of Lords held that B's 'common law' remedies would be inadequate on these facts: B could not sue in debt (7.20); and B's claim for common law compensation would be 'nominal' (for example, £5, a token sum to denote technical breach), because B's personal loss was zero on these facts (the estate's claim for substantial compensation would have been successful if B's estate had 'stepped in' and paid the sums to T; then the estate would have (legitimately) suffered loss *in its own name*). But on the facts of the *Beswick* case, 'common law remedies would have been inadequate' (on this requirement, see 18.14). It would be quite unjust, therefore, if A, having received and continued to run the coal-merchant business, were left to hide behind the common law's inability to provide an adequate remedy on these facts.⁴⁹ And so the House of Lords agreed that specific performance was necessary to fill the remedial void. However, T's capacity to intervene in this case was fortuitous: if the aunt had not been B's successor *qua* administrator, she would have remained a simple 'third party beneficiary', unable to obtain direct relief at the suit of B. T, the aunt, would then have been reliant on B's decision whether to sue A on T's behalf (no trust of a promise had arisen in this case: 7.14). If the facts of *Beswick v. Beswick* were to recur after the 1999 Act (7.34), T could obtain specific performance in her own name, whether or not T was also B's administrator.

7.23 *Damages: general rule.* 'The *Woodar* rule'⁵⁰ states that B, the promisee, can obtain compensation from A *only for B's personal loss and not for T's loss*. This means that, unless B can show personal loss, A is effectively let off the hook. Although criticised,⁵¹ this rule remains the orthodox starting point in this field.⁵² However, the rule is hedged around with numerous exceptions.⁵³

7.24 Instead of creating a set of exceptions to the basic *Woodar* rule (7.23), the common law might – and arguably should – have adopted the opposite starting point: that B

48 [1968] AC 58, HL.

49 On the underlying factors in this case, see N. Andrews, 'Does a Third Party Beneficiary Have a Right in English Law?' (1988) LS 14, 28–33.

50 Affirmed by *dicta* in *Woodar Investment Development Ltd v. Wimpey Construction UK Ltd* [1980] 1 WLR 227, 283–4, 291, 293, 297, 300, HL.

51 In *Alfred McAlpine Construction Ltd v. Panatown* [2001] 1 AC 518, 538, 544D, HL, Lord Goff doubted the proposition, drawing upon G. H. Treitel (1998) 114 LQR 527.

52 A. Burrows, 'No Damages for a Third Party's Loss' (2001) 1 *Oxford University Commonwealth Law Journal* 107, 108, cites *Beswick v. Beswick* [1968] AC 58, HL, and *White v. Jones* [1995] 2 AC 207, HL, as other instances of the *Woodar* rule.

53 In *Alfred McAlpine Construction Ltd v. Panatown* [2001] 1 AC 518, 581–2, HL, Lord Millett examined these exceptional situations.

can obtain compensation on T's behalf, *provided B is furthermore required to hand this money to T* (this might have been easily achieved, for example, by requiring B and T to be joined in the action against A, and the court requiring A to pay damages to T directly).

7.25 *The building contracts trilogy.* This trilogy of cases concerns either of the following situations: B pays for A's building work (or repair to a building). A's work is defective. A has breached his contract with B. Certainly, B has a contractual claim against A, but T, a non-party, is the true victim either (1) because T acquired title to the relevant site or building *before the breach was discovered*; or (2) because T at all stages owned the property, but B paid for the work, for T's benefit; B would act as paymaster either so that VAT could be (legitimately) avoided (as in the *Panatown* case, 7.27) or so that T, a local authority, could (again legitimately) sidestep local government borrowing restrictions upon T (as in the *Darlington* case, 7.26).

7.26 There are three cases supporting this exception to the *Woodar* rule:⁵⁴ *Linden Gardens Trust Ltd v. Lenesta Sludge Disposals Ltd* (*St Martins Property Corporation Ltd v. Sir Robert McAlpine Ltd*) (1994);⁵⁵ *Darlington Borough Council v. Wiltshier Northern Ltd* (1995);⁵⁶ and the *Panatown* case (2001).⁵⁷ These building cases extended an early nineteenth-century exception (in *Dunlop v. Lambert* (1839))⁵⁸ to the (long-standing) *Woodar* rule. The *Dunlop* case (1839) concerned the promisee's capacity to sue on behalf of a *transferee of goods*.

The problem examined in *Dunlop v. Lambert* (1839) arises when goods are damaged or lost in transit during performance of a contract of carriage between carrier A and owner B. A is liable for breach to B. But B has transferred title to the goods after the contract of carriage was formed between A and B. Thus B owned them at the start of their journey, but T, the third party, by the end. In *The Albazero* (1977),⁵⁹ the House of Lords held that the rule in the *Dunlop* case (1839) allows B to obtain damages on T's behalf only if T has no direct claim against A. Such a direct claim might arise under a bill of lading.

7.27 We now move to the context of building work, where the leading case is the *Panatown* decision (2001).⁶⁰

54 E. McKendrick, 'The Common Law at Work: The Saga of Alfred McAlpine Construction Ltd v. Panatown' (2003) 3 *Oxford University Commonwealth Law Journal* 145; G. H. Treitel, (1998) 114 LQR 527; I. Duncan Wallace, (1999) 115 LQR 394; H. Unberath, (1999) 155 LQR 535; G. McMeel, [1999] *Restitution Law Review* 21; discussion at 8.21 of *Offer-Hoar v. Larkstore Ltd* [2006] EWCA 1079; [2006] 1 WLR 2926; Treitel (12th edn, London, 2007), 14-045 (assignee's claim not capped by quantum of loss suffered by the assignor).

55 [1994] 1 AC 85, HL (summarised in the *Panatown* case, [2001] 1 AC 518, 540-2, HL).

56 [1995] 1 WLR 68, CA (summarised in the *Panatown* case, [2001] 1 AC 518, 540-2, HL).

57 [2001] 1 AC 518, HL.

58 (1839) 6 Cl & F 600, HL (Sc); on which see the *Panatown* case, [2001] 1 AC 518, 523 ff, HL.

59 [1977] AC 774, 847-8, HL, *per* Lord Diplock.

60 *Panatown* case, [2001] 1 AC 518, HL; noted by B. Coote, (2001) 117 LQR 81; A. Burrows, (2001) 1 *Oxford University Commonwealth Law Journal* 107.

In 1989, A, a construction company, agreed with B to build an office block in Cambridge for approximately £10m. At all stages, T owned the site. B was a subsidiary company of T, the true owner. T had (legitimately) used B as a financial conduit to avoid VAT on the construction contract.⁶¹ The result was that T, the site's owner, was a third party to the main building contract. A and B's contract included both an arbitration clause (committing A and B to use only arbitration rather than court proceedings, in the event of a dispute) and a liquidated damages clause, which gave B £35,000 a week for late completion.⁶²

There was also a collateral contract (a 'deed') directly between A and T, the owner, whereby A, the builder, undertook to exercise reasonable care when performing the construction work. This deed was intended to enable T to assign the benefit of the deed to a purchaser in due course (no such sale in fact occurred). T's lawyers had advised that assignment of such a deed would be necessary because T and its successors would have no action in the tort of negligence for pure economic loss, the cost of rectifying the work (and loss of rental income).⁶³

A's building work was so defective that it was not until 2003 that the offices were fit for use. A had clearly breached the building contract.

In 1992, B brought an arbitration claim against A for breach of contract, seeking (1) substantial damages for the cost of rectifying the work and (2) damages for loss of profit caused by their inability to let the commercial property. There were two reasons why B had sued A (rather than T suing A under the deed). First, the A/B contract contained a set of strict obligations, but the A/T deed merely imposed a duty of care (on the value of strict obligations, see 17.06). Secondly, only the A/B contract (and not the A/T deed) was subject to an arbitration clause. Many companies prefer arbitration to High Court litigation. Arbitration offers the twin benefits of confidentiality and the choice of decision-maker(s), whereas court proceedings take place in public and the judge is randomly selected by the court system rather than by the litigants. Arbitration also offers the prospect (sadly, not always realised) of greater efficiency and speed.⁶⁴

The *ratio* of this case (given by Lords Clyde,⁶⁵ Jauncey⁶⁶ and Browne-Wilkinson⁶⁷) was that the A/T deed precluded B from recovering substantial damages from A. This was a disaster: as in the game of snakes and ladders, the claimant, after conducting three appeals subsequent to the arbitration hearing (appeals before the High Court, Court of Appeal and finally the House of Lords), had landed on a snake and slithered down to the opening square. The majority reached this conclusion by noting an exception to

61 *Panatown* [2001] 1 AC 518, 537, HL.

62 *Ibid.*, at 554.

63 *D & F Estates Ltd v. Church Commissioners for England and Wales* [1989] AC 177, HL.

64 N. Andrews, *The Modern Civil Process: Judicial and Alternative Forms of Dispute Resolution in England* (Tübingen, 2008), chapter 12, for an outline of arbitration and its attractiveness.

65 *Panatown* [2001] 1 AC 518, 531–2, 536, HL.

66 *Ibid.*, at 567–8.

67 *Ibid.*

an exception: that the *Dunlop v. Lambert* solution only applies if T has no direct right of action against the promisor, a restriction emphasised in *The Albazero* (1977).⁶⁸ This restriction is clearly intended to protect A against double liability (successive claims by B and T). However, on the facts of the *Panatown* case, there was no prospect of A being sued twice by B and T, because B and T were corporate relatives and not strangers. The better approach would have been to regard the A/T deed as an irrelevant feature of the present facts. The *Panatown* decision had the unfortunate effect of eviscerating the contractual relations between A and B: A's *strict obligation* towards B has ceased to be enforceable by B, because of the A/T deed; and the arbitration clause between A and B has also ceased to matter because the House of Lords decision would require T to sue A in court proceedings (there being no arbitration clause within the A/T deed).

7.28 *The hypothetical question: damages earmarked for B or for T, the third party?* Having decided that B could not obtain substantial damages on T's behalf, the speeches in the *Panatown* case (2001) addressed, in elaborate *dicta*, the following point, which had now become academic: if B had been permitted to sue, might he have obtained damages in B's own name (the so-called 'broad view'); or would B instead have obtained compensation on behalf of T (the so-called 'narrow view')?

7.29 The logic of the *Dunlop v. Lambert* (1839)⁶⁹ exception (7.26) is that B is suing *on behalf of T*, and so B *must account to T* for compensation obtained from A. Lords Clyde and Jauncey in the *Panatown* case (2001) were correct to state that, when T is both owner of the site and financier of the project, B's damages claim against A must be for *compensation to remedy T's loss*: the so-called 'narrow ground' adopted by the House of Lords in the *Linden Gardens* case (1994) as an exception to the *Woodar* rule. This analysis would 'fit' both heads of claim brought by B, but economically suffered by T: *the cost of cure and loss of rental*.

7.30 However, Lords Goff⁷⁰ and Millett⁷¹ in the *Panatown* case supported the so-called 'broad view' approach: that *B should have received in his own name* damages for the 'cost of cure', the expense of rectifying the building. Although some commentators suggest that the 'broad view' was also supported by Lord Browne-Wilkinson, his comment was hesitant: 'I will assume that the broader ground is sound in law.'⁷² The 'broad view' approach can be traced to Lord Griffiths' minority speech in the *Linden Gardens* case (1994):⁷³

[1.] I cannot accept that in a contract of this nature, namely for work, labour and the supply of materials, the recovery of more than nominal damages for breach of

68 [1977] AC 774, 847–8, HL, *per* Lord Diplock.

69 (1839) 6 Cl & F 600, HL (Sc).

70 *Panatown* [2001] 1 AC 518, 546–51, HL.

71 *Ibid.*, at 585–92.

72 *Ibid.*, at 577.

73 [1994] 1 AC 85, 96–7, HL (paragraph numbering added).

contract is dependent upon the plaintiff having a proprietary interest in the subject matter of the contract at the date of breach.

[2.] In everyday life contracts for work and labour are constantly being placed by those who have no proprietary interest in the subject matter of the contract. To take a common example, the matrimonial home is owned by the wife and the couple's remaining assets are owned by the husband and he is the sole earner. The house requires a new roof and the husband places a contract with a builder to carry out the work. The husband is not acting as agent for his wife, he makes the contract as principal because only he can pay for it. The builder fails to replace the roof properly and the husband has to call in and pay another builder to complete the work. Is it to be said that the husband has suffered no damage because he does not own the property?

[3.] Such a result would in my view be absurd and the answer is that the husband has suffered loss because he did not receive the bargain for which he had contracted with the first builder and the measure of damages is the cost of securing the performance of that bargain by completing the roof repairs properly by the second builder.

Paragraph 1 of this quotation contains the uncontroversial point that B can obtain damages against A even though T is the owner of the relevant site; and paragraph 2 is unproblematic, for, if B *has already paid* for rectification of A's botched building work, B has suffered recoverable loss, and it is plainly irrelevant that T has become, or that T was always, owner of the site. However, paragraph 3 is ambiguous. It might mean (uncontroversially) that the cost of cure will be awarded provided the court is satisfied that this repair is in fact intended. An alternative reading is that B can recover the cost of cure measure of damages *in his own name, no legal strings being attached, so that B can then use that sum howsoever he wishes*. We will call this last approach the 'radical broad view'. The other judges in the *Linden* case (1994) had sensibly refrained from endorsing this last-mentioned approach.

- 7.31 The 'radical broad view' is not the law. Burrows, a leading authority, says that, if B were to retain the cost of cure compensation in his own name, this would be absurd and wrong in principle, for a breach of contract is not necessarily a ground for awarding substantial loss,⁷⁴ merely a basis for nominal damages. To gain 'substantial damages', the claimant must prove actual loss.⁷⁵ *This must be B's loss, unless an exception to the Woodar rule (7.23) applies*. Burrows' analysis is consistent with remarks by Judge Toulmin QC in *Mirant Asia-Pacific Construction (Hong Kong) Ltd v. Ove Arup & Partners International Ltd* (2007): that B cannot receive the cost of cure measure of damages

74 A. Burrows, 'No Damages for a Third Party's Loss' (2001) 1 *Oxford University Commonwealth Law Journal* 107, 109 ff.

75 *Ibid.*, at 113.

unless he can show that *this money has already been used, or will be used, to effect the necessary repair*. The judge said:⁷⁶ '[T]he court has ... to be satisfied that the claimants are seeking compensation for a genuine loss and not seeking an uncovenanted profit. The court must also be satisfied ... that the damages represent a genuine and quantifiable loss to [the promisee].' Thus, even if it was B who financed the building work (for example, B is a philanthropist who had paid for a new thatched roof on a village hall),⁷⁷ B cannot recover the cost of cure measure unless (1) B has already incurred the cost of rectifying the consequences of A's breach, or (2) B is legally committed to incurring that cost, or (3) B satisfies the court that he intends to use a cost of cure fund to carry out such repairs.

The prospect of B being allowed to pocket a 'cost of cure award' becomes even more grotesque if it was T who financed the initial building contract. This was the situation in the *Panatown* case, where even the so-called 'broad view' proponents, Lords Goff and Millett, devised arguments to ensure that B would hold the cost of cure for the benefit of T, who had initially financed the project. Lord Millett suggested that B's substantial damages would 'almost certainly be held on trust to apply them at the direction of the group company [T] which provided the building finance'.⁷⁸ Employing a similar technique, Lord Goff contended that B would be obliged under an implied term to hand this money to T.⁷⁹ All of this shows that the compensatory searchlight should be aimed at T, the owner of the site and the financier of the building work.

Another problem with the 'radical broad view' is that it would not work at all in situations concerning loss of rental suffered when a commercial property is finished very late. This was the second possible head of claim in the *Panatown* case (2001) (the A/B contract contained a liquidated damages clause quantifying compensation under this head). It would make no sense to attribute this loss to B, who had no power to grant leases of the building. It follows, therefore, that the House of Lords would have had to allow B to recover liquidated damages under the A/B contract and hold them for T's benefit (but, as we have seen, the *ratio* in that case, criticised above, was that the A/T deed precluded a claim by B against A, 7.27).

7.32 To sum up, when B has entered into a building contract concerning T's land (T being the transferee of the site, or the owner at all stages):

- (1) B should be able to recover damages on T's behalf; this is the so-called 'narrow view' and the *ratio* of the *Linden Gardens* case (1994).⁸⁰
- (2) The courts should be slow to apply the *Albazero* restriction⁸¹ just because T has a direct contractual right of action against A; instead, the court should assess whether

76 [2007] EWHC 918 (TCC); [2008] Bus LR D1, at [630] (referring also, *ibid.*, at [625], to his discussion of the *Panatown* case in *Catlin Estates Ltd v. Carter Jonas* [2005] EWHC 2315 (TCC); [2006] PNLR 273).

77 *Panatown* [2001] 1 AC 518, 559–600, HL, *per* Lord Goff.

78 *Ibid.*, at 592.

79 *Ibid.*, at 560.

80 [1994] 1 AC 85, 96–7, HL.

81 [1977] AC 774, 847–8, HL, *per* Lord Diplock.

there is a realistic risk of double compensatory awards against A by B and T in turn; procedural joinder of B and T will guard against that risk.

- (3) B should be regarded as suing in B's own name (as distinct from suing on T's behalf) if B has already effected the repairs (his personal loss is then evident; see 7.30, paragraph 2 of Lord Griffiths' passage from the *Linden Gardens* case) or B has committed himself under contract with a new builder to have the repair work done (again, B's personal loss is evident).
- (4) Finally, there is the situation where no repair work has yet been undertaken, and B has not contracted to have the work done; here, the court must be satisfied that B is intent on using a cost of cure fund to remedy the relevant defects (generally on the cost of cure measure, see 18.27 to 18.30); otherwise, the court runs the triple risk of over-compensating B, of under-protecting T, and of penalising A (who is made to pay for a cure not in fact desired or achieved). If B is clearly intent on using the cost of cure damages to finance repair work, by procuring that work himself, B should be entitled to recover that cost of cure under the broad view – the award being made in anticipation of B's financial shortfall. Whereas, if B's intention is to use the cost of cure by handing the money to T, T then using the fund to finance repair work, B is entitled to the cost of cure measure in accordance with the narrow view, since B will not suffer any personal financial shortfall. These remarks are consistent with Lord Griffiths' comment in the *Linden Gardens* case (1994):⁸² 'The court will of course wish to be satisfied that the repairs have been or are likely to be carried out but if they are carried out the cost of doing them must fall upon the defendant who broke his contract.'

7.33 *Two more remedies: a declaration and a stay of proceedings.* Finally, if A has promised B that *A will not bring proceedings against T*, B might be able to obtain a declaration or 'stay' of the proceedings (thereby halting those proceedings) to protect the intended third party. *Snelling v. John Snelling Ltd* (1973) illustrates this (see the text below).⁸³ When seeking such a declaration or stay, B must show that the relief is necessary to protect his own legitimate interest.⁸⁴

In the *Snelling* case (1973), a family company owed large sums to each of three brothers, who were directors and shareholders.⁸⁵ The brothers agreed amongst themselves that, if one of them resigned as director, he would forfeit the sum owed to him by the company and that he would not sue the company for that money (but the company was not a party to this agreement not to sue; it was a third party 'beneficiary' of that agreement). One of the brothers did resign. He then reneged on the promise not to sue the company.

Ormrod J gave a declaration (no injunction can be granted to restrain any proceedings in the High Court)⁸⁶ that the proceedings should be stayed. He noted that the company ('T') and the

⁸² [1994] 1 AC 85, 97, HL.

⁸³ [1973] QB 87, Ormrod J.

⁸⁴ *Gore v. Van der Lann* [1967] 2 QB 31, CA.

⁸⁵ [1973] QB 87, Ormrod J.

⁸⁶ *Gore* case, [1967] 2 QB 31, CA; see now section 49(2) of the Senior Courts Act 1981.

other two brothers ('B') were privy to the litigation as co-defendants. If the company alone had been a defendant, it would have lacked a good defence because (in accordance with the common law privity doctrine) it was not party to the fraternal contract not to sue. However, in this situation, it would now be possible for T, if wrongfully sued by A, to obtain under the 1999 Act (7.34) a declaration or a stay (thereby halting the wrongful proceedings) without T having to rely on B to intervene as a party to the wrongful proceedings to seek a stay on T's behalf.

6. THE CONTRACTS (RIGHTS OF THIRD PARTIES) ACT 1999⁸⁷

7.34 The Act enables T to obtain a direct right of action against A. As we shall see, this direct right of action arises if (1) A and B expressly confer this right on T, or (2) if A and B's contract 'purports to confer a benefit' on T and there is no contrary indication to negative an implied wish that T should have a direct right of action against A. The Act's direct right of action co-exists with B's right of action against A at common law (on which see the preceding section 5 of this chapter at 7.19 onwards). Commentators refer to (1) as 'limb 1' and to (2) as 'limb 2' (7.39 to 7.42).

7.35 The Act applies to most transactions. But there are five classes of contract where it was felt that the Act might unduly interfere with a settled scheme of rules:⁸⁸

- (1) contracts in bills of exchange, promissory notes or other negotiable instruments;⁸⁹
- (2) contracts falling within section 14 of the Companies Act 1985;⁹⁰
- (3) terms in contracts of employment purporting to enable a third party to sue an employee, or in a worker's contract to sue a 'worker', or in a relevant contract against an agency worker;⁹¹
- (4) terms purporting to enable a third party to sue in the case of carriage of goods by sea;⁹²
- (5) carriage of goods by rail, road or air, where an international transport convention applies.⁹³

87 N. Andrews, 'Strangers to Justice No Longer: The Reversal of the Privity Rule under the Contracts (Rights of Third Parties) Act 1999' [2001] CLJ 353–81; H. Beale, 'A Review of the Contracts (Rights of Third Parties) Act 1999', in A. Burrows and E. Peel (eds.), *Contract Formation and Parties* (Oxford, 2010); A. S. Burrows, [2000] LMCLQ 540–54; C. MacMillan, (2000) 63 MLR 721–38; R. Stevens, (2004) 120 LQR 292–323 (who bemoans its enactment); M. Smith, *The Law of Assignment* (Oxford, 2007), chapter 4; Law Commission, *Privity of Contract: Contracts for the Benefit of Third Parties* (Law Commission Report No. 242, Cm 3329, London, 1996), notably Parts VII–XI; V. V. Palmer, 'Contracts in Favour of Third Persons in Europe' (2003) 11 *European Review of Private Law* 8–27.

88 *Treitel* (12th edn, London, 2007), 14–119 and 14–120.

89 Section 6(1) of the 1999 Act.

90 Section 6(2) of the 1999 Act. Section 14 of the Companies Act 1989 ('Effect of memorandum and articles') is now section 33 of the Companies Act 2006.

91 Section 6(3) and (4).

92 Section 6(5)(a), (6) and (7); the Carriage of Goods by Sea Act 1924 already deals with third party rights of positive suit in this context.

93 Section 6(5)(b) and (8) of the 1999 Act; Law Commission, *Privity of Contract: Contracts for the Benefit of Third Parties* (Law Commission Report No. 242, Cm 3329, London, 1996), 12.12 ff.

Categories (1) to (3) are wholly unaffected by the new legislation. Categories (4) and (5) are unaffected by the 1999 Act as far as active claims by the third party are concerned: but, in the case of categories (4) and (5), terms conferring the benefit of exemption clauses on third parties are covered by the 1999 Act (this 'exception to an exception' is a point of great importance: see 7.62 below).

7.36 Commencement. For most contracts, the 1999 Act first operated only from 11 May 2000 (although slightly earlier contracts could expressly incorporate the Act).⁹⁴

7.37 Naming or other identification of third parties. Section 1(3) of the Act states:

The third party must be expressly identified in the contract by name, as a member of a class or as answering a particular description but need not be in existence when the contract is entered into.

The provision makes clear that T need not exist when the contract is formed. Therefore, third parties under the Act can include future companies or children not yet born, or indeed not yet conceived.

7.38 Section 1(3) (see above) recognises three modes of identifying T: where T is: (1) 'expressly identified in the contract by name'; or (2) 'as a member of a class'; or (3) 'as answering a particular description', for example, 'employees of B' or 'sub-contractors and agents of B'. Modes (2) and (3) were considered by the Court of Appeal in *Avraamides v. Colwill* (2006):⁹⁵

In a direct two-party contract between B and T, B had earlier contracted to refurbish T's two bathrooms. By a separate transaction, a 'transfer agreement' between A and B, A received B's assets and A assumed B's liabilities. The relevant clause provided: 'The purchaser undertakes to complete outstanding customer orders ... and to pay in the normal course of time any liabilities properly incurred by the company as at 31 March 2003.' T contended that this meant that A had assumed responsibility for B's imperfect performance of B's contract with T. But the Court of Appeal, applying the present requirement that T has to be expressly identified in the contract by name, by class or by description, regarded A and B's agreement as too vague to satisfy this test. It could not be restricted to 'customers' because the phrase 'liabilities properly incurred' extended the field of possible beneficiaries to an impermissibly wide extent.

Waller LJ (Leveson LJ agreeing) said⁹⁶ that 'expressly identified' in section 1(3):

simply does not allow a process of construction or implication ... The benefit from the obligation to pay liabilities properly incurred would benefit third parties but of a large number of unidentified classes.

⁹⁴ Section 10(2) and (3) of the 1999 Act.

⁹⁵ [2006] EWCA Civ 1533; [2007] BLR 76.

⁹⁶ *Ibid.*, at [19].

7.39 *Test for identifying a third party's rights.* Subsections 1(1) and 1(2) of the Act state:

- (1) Subject to the provisions of this Act, a person who is not a party to a contract (a 'third party') may in his own right enforce a term of the contract if—
 - (a) the contract expressly provides that he may, or
 - (b) subject to subsection (2), the term purports to confer a benefit on him.
- (2) Subsection (1)(b) does not apply if on a proper construction of the contract it appears that the parties did not intend the term to be enforceable by the third party.

Thus, a statutory third party right will arise if *either*:

Limb 1 A and B have expressly stated that T should have a right of action against A (see further the next paragraph);

or

Limb 2 the contract between A and B 'purports to confer a benefit on' the third party and A fails to show any reason to negative T's presumptive direct right of action against A (see further 7.41 and 7.42).

7.40 As for limb 1, T might enjoy a right of action even though T is not personally benefited by A's performance, because T is to take as trustee for X.⁹⁷ Limb 1 might also be used to confer on a third party the *benefit of an exclusion clause*, section 1(6) providing (see further 7.59 ff):

Where a term of a contract excludes or limits liability in relation to any matter references in this Act to the third party enforcing the term shall be construed as references to his availing himself of the exclusion or limitation.

7.41 As for limb 2, subsections 1(1)(b) and 1(2) involve a two-stage inquiry: (1) where A and B's contract 'purports to confer' on T a 'benefit' (see further 7.41), this promise or clause is deemed furthermore to confer a right of action on T against A (or, in the case of the shield contained within an exclusion clause, T can take advantage of an exemption clause); (2) *unless* on a 'proper construction of the contract it appears that the parties did not intend the term to be enforceable by the third party'. This two-step approach was adopted by Colman J in *Nisshin Shipping Co. Ltd v. Cleaves & Co. Ltd* (2004),⁹⁸ and approved by the Court of Appeal in the *Laemthong* case (2005).⁹⁹

97 P. Kincaid, (1997) 12 *Journal of Contract Law* 47, 49, 55; Law Commission, *Privity of Contract: Contracts for the Benefit of Third Parties* (Law Commission Report No. 242, Cm 3329, London, 1996), 7.5 and 7.12 to 7.16.

98 [2004] EWHC 2602 (Comm); [2004] 1 Lloyd's Rep 38.

99 *Laemthong International Lines Co. Ltd v. Abdullah Mohammed Fahem & Co.* [2005] EWCA Civ 519; [2005] 2 All ER (Comm) 167.

7.42 According to the Law Commission,¹⁰⁰ limb 2 will require a distinction to be drawn between a direct beneficiary and an ‘incidental’ one, and this would mean that limb 2 *would not be satisfied* on facts similar to *White v. Jones* (1995) (which antedated the Act).¹⁰¹ That case concerned a contract between solicitor and client for the amendment of the client’s will by codicil. The client wanted to add his two daughters, Pauline and Carole, as legatees, giving them £9,000 each. The solicitor went on holiday. By the time he returned, the testator had died and so it was too late to effect valid legacies by codicil. The prospective legatees sued the solicitor in the tort of negligence. The House of Lords, by a majority of three to two, held that the claim should succeed. The defendant solicitor had been negligent and a duty of care should be recognised in this context. Otherwise, professional negligence would go unremedied. But, in the Law Commission’s view, commenting on *White v. Jones* (1995), the intended legatees are not direct third party beneficiaries, but merely ‘incidental’ beneficiaries. This is because A, the solicitor, agreed to confer the benefit of professional services on B, the testator, who was the *primary* beneficiary. A’s performance in carrying out the changes to B’s will would only incidentally benefit the intended legatees. And so, such a third party is a merely *incidental beneficiary* lying outside the compass of the ‘limb 2’ provision (explained above).¹⁰² Furthermore, Clarke J in *Dolphin Maritime & Aviation Services Ltd v. Sveriges Angfartygs Assurans Forening* (2009)¹⁰³ said: ‘[P]urporting to “confer” a benefit seems to me to connote that the language used by the parties shows that one of the purposes of their bargain (rather than one of its incidental effects if performed) was to benefit the third party’. Therefore, he distinguished¹⁰⁴ between (1) an arrangement whereby A was obliged to pay B, or to make payment to B’s agent, and (2) a situation where A and B agreed that A should pay C. In situation (1), B’s agent is not a beneficiary under limb 2 of the 1999 Act, but merely a conduit for possible payment, for the intended and lasting pecuniary benefit of B, the principal.

7.43 *Third party’s remedies.* If T has a right of action under the Act, he can employ (as appropriate) the remedies of debt, specific performance, damages, etc. (for an overview of remedies for breach of contract, see 18.02) in accordance with common law and equitable principles. Section 1(5) of the Act states:

For the purpose of exercising his right to enforce a term of the contract, there shall be available to the third party any remedy that would have been available to him in an action for breach of contract if he had been a party to the contract (and the rules relating to damages, injunctions, specific performance and other relief shall apply accordingly).

100 Law Commission, *Privity of Contract: Contracts for the Benefit of Third Parties* (Law Commission Report No. 242, Cm 3329, London, 1996), 7.19 ff.

101 [1995] 2 AC 207, HL.

102 Law Commission, *Privity of Contract: Contracts for the Benefit of Third Parties* (Law Commission Report No. 242, Cm 3329, London, 1996), 7.19 ff; cf *Beswick v. Beswick* [1968] AC 58, HL (A promises B to pay T: 7.22).

103 [2009] EWHC 716 (Comm); [2010] 1 All ER (Comm) 473; [2009] 2 Lloyd’s Rep 123; [2009] 1 CLC 460, at [74].

104 *Ibid.*, at [76].

7.44 Specific performance. In the case of the remedy of specific performance (7.19 and 7.20; more generally see 18.13 ff), the Act creates an exception to the general maxim of equity that specific performance can only be awarded in favour of someone who has provided consideration ('equity does not assist a volunteer', that is, a gratuitous promisee or beneficiary). The Act states that T can obtain 'specific performance'. But this must presuppose that B has furnished consideration and that the remedy of specific performance is justified on the facts because debt or damages would be insufficient to protect T. Thus, after the Act, the widow in *Beswick v. Beswick* (1968) (see 7.22 above) could now obtain specific performance *in her own name* as a third party.¹⁰⁵

7.45 Damages. As for T's claims for damages, protection under the Act extends not just to his 'reliance loss' (out-of-pocket losses incurred in the belief that the contract would not be breached) but includes his 'expectation interest' (that is, the financial or other material gain that would have been achieved if the promisor had not breached the contract – generally on these types of compensatory measures, see 18.25).¹⁰⁶

7.46 Right of defence or set-off connecting A and T. If A is sued by T, A can raise against T any 'defence or set-off' or 'counter-claim' pertaining *as between A and T directly* (unless the contract provides otherwise).¹⁰⁷ If, for example, the A/B contract provides that A should pay T £1m, but in a separate transaction T had incurred a debt to A of £100,000, satisfaction of T's claim against A under the Act will be reduced to take into account (by way of 'set-off') the latter sum. Section 3(4) of the Act states:

The promisor shall also have available to him—

- (a) by way of defence or set-off any matter, and
- (b) by way of counter-claim any matter not arising from the contract,

that would have been available to him by way of defence or set-off or, as the case may be, by way of counter-claim against the third party if the third party had been a party to the contract.

7.47 Right of defence or set-off connecting A and B. T's right of action is *subject to the same rights of defence or set-off that A would enjoy if A had instead been sued by B* under the same contract (unless the contract provides otherwise). Section 3(2) of the Act makes this clear:

The promisor shall have available to him by way of defence or set-off any matter that—

- (a) arises from or in connection with the contract and is relevant to the term, and
- (b) would have been available to him by way of defence or set-off if the proceedings had been brought by the promisee.

¹⁰⁵ [1968] AC 58, HL.

¹⁰⁶ Law Commission, *Privity of Contract: Contracts for the Benefit of Third Parties* (Law Commission Report No. 242, Cm 3329, London, 1996), 9.33.

¹⁰⁷ See section 3(5) of the 1999 Act for this last point.

The following scenarios illustrate how section 3(2) of the Act works:

- (1) *Defence (A/B contract voidable)*. If B makes a misrepresentation which entitles A to rescind the contract (for the remedy of rescission in this context, see 9.18), and T sues A under the Act, section 3(2) (quoted in the previous paragraph) allows A to raise against T the defence of rescission.
- (2) *Defence (condition precedent to A's liability)*. Here, A has promised to pay £1,000 to T *if B first pays £5,000 to T*, and B has defaulted; T sues A under the Act; section 3(2) allows A to raise the defence that B's performance is a condition precedent to A's duty to pay.
- (3) *Set-off*. Suppose that, in clause 99 of a contract, A has promised B to pay £2m to T; but B has incurred a debt to A of £1m under clause 98 of the same contract. Section 3(2) would allow A to set off the £1m owed by B to A when T asks A to pay T the £2m. This is because that right of set-off 'arises from ... the contract' between A and B in which T is also to be benefited. But *it would be different if* the £1m owed by B to A arose under *a separate contract* having no factual connection with the A/B/T contract. In this last situation, T's action against A would not be subject to A's set-off.
- (4) *Defence or set-off: further permutation*. Section 3(2) is the 'default' rule concerning defences and set-off. That default position will not apply if section 3(3) applies. Section 3(3) provides that, *if A and B expressly stipulate*, A can enjoy any defence against T's action, *including any right of set-off*, that A would have *vis-à-vis* B. Section 3(3) will then widen the scope of set-off available to A, so as to cover all sums owed by B to A, even if the relevant liability arose *outside and has no connection with the A/B/T transaction* (see the narrow wording of section 3(2), set out above).

7.48 Variation or rescission of the contract.¹⁰⁸ Section 2(1) of the Act provides:

Subject to the provisions of this section, where a third party has a right under section 1 to enforce a term of the contract, the parties to the contract may not, by agreement, rescind the contract, or vary it in such a way as to extinguish or alter his entitlement under that right, without his consent if—

- (a) the third party has communicated his assent to the term to the promisor,
- (b) the promisor is aware that the third party has relied on the term, or
- (c) the promisor can reasonably be expected to have foreseen that the third party would rely on the term and the third party has in fact relied on it.

And so, in general, A and B will retain the power to vary or 'rescind' the contract without T's consent. As noted by the present author in a journal article,¹⁰⁹ the Law Commission

¹⁰⁸ N. Andrews, 'Strangers to Justice No Longer: The Reversal of the Privity Rule under the Contracts (Rights of Third Parties) Act 1999' [2001] CLJ 353, 361 ff.

¹⁰⁹ Andrews, [2001] CLJ 353, 362, noting Law Commission, *Privity of Contract: Contracts for the Benefit of Third Parties* (Law Commission Report No. 242, Cm 3329, London, 1996), 946; and noting Burrows'

said that A and B cannot create from the outset an irrevocable set of rights for T's benefit, although that view has been subsequently contradicted by Burrows. It is submitted that Burrows is right to suggest that an agreement which explicitly stipulates that a third party will enjoy a right under the Act without needing to consent to it, and that this right will not be revocable by A and B, should take effect as an irrevocable right. Subject to that possibility, A and B will retain the right 'by agreement, [to] rescind the contract, or vary it in such a way as to extinguish or alter [the third party's] entitlement'. My article noted¹¹⁰ that A and B will 'by agreement rescind ... or vary' the contract if A and B for consideration so agree, or if B by deed so agrees:¹¹¹ but here T will have already gained protection from this unfavourable cancellation or variation if: (1) T has communicated 'assent to the term' to A; or (2) T has relied on A's promise; T's reliance will count if A knew that it had occurred, or at least if it was reasonably foreseeable by A (the Law Commission said that T's reliance need not be 'detrimental').¹¹² These are the 'cut-off points' at which A and B cease to be able 'by agreement' to 'rescind or vary' the contract so as to diminish or terminate T's interest.

However, these cut-off points are irrelevant if any of the following occurs (situations (1) to (3) do not constitute examples of a contract, or part of it, being rescinded or varied 'by agreement'; and situation (4) is also outside the scheme for protecting T):

- (1) a decision by A to terminate the contract following B's breach;
- (2) A's decision to rescind the contract following B's misrepresentation, undue influence, non-disclosure (for example, in the case of insurance contracts);
- (3) nor can A and B be said to have terminated a contract 'by agreement' if the contract is terminated by operation of law following a frustrating event;
- (4) furthermore, the third party cannot continue to assert rights against A if the contract, or a part of it, ceases to operate, or is suspended, in accordance with a *force majeure* clause (12.02 at (16)); this is because section 1(4) of the Act states: 'This section does not confer a right on a third party to enforce a term of a contract otherwise than subject to and in accordance with other relevant terms of the contract.'

7.49 *Manifestation of assent.* Section 2(2) of the Act specifies how T's 'assent' can be manifested:

The assent referred to in subsection (1)(a)–

- (a) may be by words or conduct, and

contradiction of this in [2000] LMCLQ 540, 547 n. 22, pointing to the wide language of section 2(3)(b) of the 1999 Act, which provides: '[Subsection 2(1)] is subject to any express term of the contract under which (a) the parties to the contract may by agreement rescind or vary the contract without the consent of the third party, or (b) the consent of the third party is required in circumstances specified in the contract instead of those set out in subsection (1)(a) to (c).'

110 N. Andrews, [2001] CLJ 353, 363–6.

111 As noted, *ibid.*, at 365, if B does not cancel or vary the substantive relations between A and B but merely covenants not to sue A for breach or default, such an undertaking becomes binding on B but does not purport to fetter T's rights under the 1999 Act against A.

112 Law Commission, *Privity of Contract: Contracts for the Benefit of Third Parties* (Law Commission Report No. 242, Cm 3329, London, 1996), 9.19.

- (b) if sent to the promisor by post or other means, shall not be regarded as communicated to the promisor until received by him.

'Assent', if successfully communicated by T, need not be accompanied by 'reliance' on T's part. The Act also makes clear that the postal rule (3.18) *will not* apply to T's posted acceptance. And so T's 'assent' must be *received* by A. For example, on Tuesday, A and B agree that A will pay T £5,000 a month; on Wednesday, T posts a letter to A 'assenting' to this proposed payment; on Thursday, A and B agree to terminate the contract and B successfully sends T an e-mail, notifying T of this cancellation; T's letter of 'assent' arrives too late, on Friday.

- 7.50 *'Master clause' in favour of A and B.* A and B can insert a 'master clause' in the contract for the purpose of retaining the power to vary or extinguish T's putative rights. This clause will prevent T from gaining an irrevocable right against A. The effect is that A and B will have 'contracted out' of the general approach just summarised. Such a master clause (1) must be 'express'; (2) it must form part of the main contract ('term of the contract ...'); and (3) any exercise of this power should involve A and B acting 'by agreement [to] rescind or vary the contract'. Section 2(3) provides:

Subsection (1) is subject to any express term of the contract under which–

- (a) the parties to the contract may by agreement rescind or vary the contract without the consent of the third party, or
- (b) the consent of the third party is required in circumstances specified in the contract instead of those set out in subsection (1)(a) to (c).

- 7.51 *Clause permitting variable selection of third party.* Treitel suggests that T's 'assent' or 'reliance' on A and B's promise (in the manner just explained) will make no difference if the terms of A's obligation were expressed to be subject to B's direction, for example, if A promises B to pay £x to *T1 or T2, as B decides*, or A promises B to pay to *Q1 or, if B later prefers, Q2*.¹¹³ Treitel says: 'in such a case ... the contract is not varied. On the contrary, it is performed in accordance with its original terms, under which B has a choice as to the person to whom performance is to be rendered.' In other words, T1 or Q1 could not acquire irrevocable rights by 'assent' to A or reliance on A's promise. Another way of reaching the same conclusion (a right to alter A's performance without T enjoying a power to preclude this) is to treat such an elective clause as a variation of the contract (contrary to Treitel's argument). On this view, B's power of direction rests on an 'express term' of the contract.

- 7.52 *Common law rights of promisee preserved.* Section 4 of the Act states: 'Section 1 does not affect any right of the promisee to enforce any term of the contract.' And so T's rights under the Act apply in parallel to B's existing common law right to sue A for breach of

¹¹³ Treitel (12th edn, London, 2007), 14–110.

contract (see 7.19 to 7.33 above). Thus, the following actions by promisees remain available: (1) claims for damages made by the promisee to protect a third party to receive compensation will continue to have great importance (see the *Panatown*¹¹⁴ line of cases, 7.25); and (2) claims for specific performance at the suit of B. As for (2), the facts of *Beswick v. Beswick* (1968)¹¹⁵ (7.22) would now involve two alternative routes to justice: B (the uncle's estate) could still sue A and obtain specific performance on those facts, as the House of Lords held in that case; or T, the widow, could sue A directly under limb 2 (7.41) of the Act and obtain *specific performance* without relying on B to take the initiative.

7.53 *Parallel third party rights of action not ousted.* Section 7(1) of the Act preserves 'any right or remedy of a third party that exists or is available apart from the Act'. This refers to any other statutory right or trust-of-a-promise entitlement enabling T to sue A directly. We will return to this overlap in discussion of the *Nisshin* case at 7.58.

7.54 *Rule excluding 'double compensation' for the same loss.* Section 5 of the Act prevents A being at risk of 'double jeopardy' for the same loss, that is, liability to B at common law and liability to T in a claim brought under the Act. Section 5 provides:

Where under section 1 a term of a contract is enforceable by a third party, and the promisee has recovered from the promisor a sum¹¹⁶ in respect of—

- (a) the third party's loss in respect of the term, or
- (b) the expense to the promisee of making good to the third party the default of the promisor,

then in any proceedings brought in reliance on that section by the third party, the court shall reduce any award to the third party to such extent as it thinks appropriate to take account of the sum recovered by the promisee.

Three issues arise. First, this provision does not bar a second action by T, but merely instructs the relevant tribunal not to award a double measure of compensation in respect of the same loss.¹¹⁷ The draftsman seems to have had in mind a 'follow-up' action by T to gain the 'cost of cure' measure of damages, B having already been awarded this sum at common law. Here, section 5 would prevent A from having to pay both B and T the *double* cost of rectifying the defective building on facts similar to the *Panatown* case (7.27). Secondly, if B sues first and fails to obtain relief in respect of his loss, the Act does not prevent T from *successfully suing* A in a second action in respect of the same breach. Successive judgments, by B and T, are possible, although double recovery by B and T is prevented. Finally, there is the question, 'what if T sues A first and then B sues A?' Here, the Act is silent. The Law Commission thought this

¹¹⁴ [2001] 1 AC 518, HL.

¹¹⁵ [1968] AC 58, HL.

¹¹⁶ The phrase 'sum recovered' would not include a non-monetary order (specific performance, injunction, declaration, etc.).

¹¹⁷ On this point, see the preceding footnote.

a ‘non-problem’, and commented: ‘Nor will there be a problem if the third party first recovered damages because then the promisee would be left with no corresponding loss outstanding.’¹¹⁸

7.55 *Limitation of actions.* Section 7(3) applies the contractual limitation periods to claims by the third party founded upon the present Act: six years for ordinary (‘simple’)¹¹⁹ contracts and twelve years for deeds (5.03).¹²⁰

7.56 *Exclusion of the Act by the contracting parties.* A and B can insert a clause which excludes the Act, for example:

The parties to this agreement do not intend that any term of this agreement shall be enforceable by any person who is not a party to this agreement and, accordingly, section 1(1)(b) of the Contracts (Rights of Third Parties) Act 1999 does not apply to any term of this agreement (and any amendments, alterations or supplements to it).

The Act does not spell out this possibility. But the power is implicit and the Law Commission itself discussed this.¹²¹ In fact, many commercial documents contain a clause excluding the Act. This avoids doubt whether non-parties were intended to acquire rights under limb 2 of the Act (7.41).

7.57 *Dispute concerning ‘limb 2’.* *Prudential Assurance Co. Ltd v. Ayres* (2008) illustrates the potential snag of a contest concerning limb 2 (7.41).¹²² The case concerned a lease containing a special term shielding the tenant partnership from ordinary liability for rent. The judge at first instance (Lindsay J) had upheld a claim based on limb 2 of the 1999 Act. In his view, this clause ‘purported’ to benefit a third party, Z, an assignee of the relevant lease. Fortunately, on appeal, this curious result was reversed. The Court of Appeal held that the contract’s reference to a third party was a drafting error.

7.58 *Arbitration clauses and the 1999 Act.* Section 8(1) of the Act (introduced at the eleventh hour of the Parliamentary process to deal with arbitration¹²³ disputes arising under the Act) states:

(1) Where—

(a) a right under section 1 to enforce a term (‘the substantive term’) is subject to a term providing for the submission of disputes to arbitration (‘the arbitration agreement’), and

¹¹⁸ Law Commission, *Privity of Contract: Contracts for the Benefit of Third Parties* (Law Commission Report No. 242, Cm 3329, London, 1996), 11.16.

¹¹⁹ Section 5 of the Limitation Act 1980.

¹²⁰ Section 8 of the Limitation Act 1980 refers to actions on ‘specialties’, for example, a deed.

¹²¹ Law Commission, *Privity of Contract: Contracts for the Benefit of Third Parties* (Law Commission Report No. 242, Cm 3329, London, 1996), 7.18(iii).

¹²² [2008] EWCA Civ 52; [2008] 1 All ER 1266 (reversing Lindsay J).

¹²³ N. Andrews, *The Modern Civil Process: Judicial and Alternative Forms of Dispute Resolution in England* (Tübingen, 2008), chapter 12, for an outline of arbitration and its attractiveness.

(b) the arbitration agreement is an agreement in writing for the purposes of Part 1 of the Arbitration Act 1996,

the third party shall be treated for the purposes of that Act as a party to the arbitration agreement as regards disputes between himself and the promisor relating to the enforcement of the substantive term by the third party.

Colman J in *Nisshin Shipping Co. Ltd v. Cleaves & Co. Ltd* (2003)¹²⁴ held that section 8(1) allows T to sue A in an arbitration *if there is an arbitration clause in A and B's contract* (such a clause normally *obliges* A and B to adopt arbitration as their chosen method of dispute resolution, rather than litigation in the courts). Indeed, Colman J suggested, without having to decide this further point, that arbitration is a mandatory route for T in this situation.¹²⁵

In *Nisshin Shipping Co. Ltd v. Cleaves & Co. Ltd* (2003),¹²⁶ B chartered A's ship and T brokered this deal. The charterparty stated that T should receive a specified commission payable by A. The charterparty further provided that 'any dispute arising' between A and B should be referred to arbitration (rather than to litigation in the courts). On the facts of this case, and as conceded by counsel on the basis of House of Lords authority directly in point,¹²⁷ T also had (in addition to the 1999 Act right of action) a right under a trust of a promise to sue A (B having defaulted in his trustee duty to sue A on T's behalf) (7.14).

Colman J held that T's action under the 1999 Act could be brought by arbitration, as stated in section 8(1) (cited at 7.58 above). The arbitration would then be between T and A. There would be no need for T to join B as a party to the arbitration reference.

But section 8(1) would not help T to bring the trust of a promise claim because that subsection is only concerned with claims against A founded on section 1 of the 1999 Act. And so an action by T under the trust of a promise doctrine could not be arbitrated (the arbitration clause only applying as between A and B, and so the arbitrator would lack jurisdiction to hear a claim brought by T).

If T chose to sue A under a trust of a promise in court proceedings, joinder of A, B and T would be required (unless waived by A: see 7.14 at (4) above). But it is unclear whether A would be entitled to a stay of those proceedings by contending that B (contrary to the commitment made by both A and B that they would only use arbitration and not resort to litigation) would be illegitimately participating in those court proceedings.

124 [2003] EWHC 2602 (Comm); [2004] 1 Lloyd's Rep 38.

125 *Ibid.*, at [44].

126 *Ibid.*

127 *Les Affréteurs Réunis SA v. Leopold Walford (London) Ltd* [1919] AC 801, HL (applying *Robertson v. Wait* (1853) 8 Ex 299 which had given effect to an implied trust of a promise in this mercantile context).

7. THE BENEFIT OF EXCLUSION CLAUSES AT COMMON LAW AND UNDER THE 1999 ACT

7.59 *Common law saga: the privity rule and the benefit of exclusion clauses.* In *Scruttons v. Midland Silicones* (1962), the House of Lords held that the privity doctrine prevents T from gaining any rights under a contract to which he is a stranger, even the ‘passive’ protective rights of an exclusion clause.¹²⁸

The usual context is that A and B have agreed that A will not be free to sue T in tort (or, at least, that T’s liability to A will be capped, or subject to a time bar) if T carelessly damages A’s goods while they are in transit. The House of Lords in the *Scruttons* case held that the confusing decision in *Elder Dempster & Co. Ltd v. Paterson Zochonis & Co.* (1924) had not recognised a doctrine of ‘vicarious immunity’, that is, a doctrine allowing T to shelter by operation of law behind B’s explicit immunity (by exclusion clause) against liability in tort towards A.¹²⁹

The ‘no shield to a third party’ aspect of the *Scruttons* decision (1962) was widely criticised, and Lord Denning persuasively dissented in the case itself. The majority’s decision involved two problems: (1) it was unconvincing in principle; and (2) it did not make commercial sense, because it increased the cost of insurance cover and hence increased the charges made for freight services.

7.60 As for (1), the first problem, the House of Lords in the *Scruttons* case (1962)¹³⁰ gave no convincing justification for this decision to extend privity reasoning beyond the context where T is *seeking to sue A* to the distinct context where *T is seeking to be protected against an action by A*. As noted at 7.07 and 7.08, T’s inability to *sue A* has been judicially rationalised on three grounds: (i) ‘only a party can sue’, (ii) ‘only a person who has provided consideration can sue’, and (iii) the need not to fetter A and B’s powers to revoke or vary their agreement. But points (ii) and (iii) do not apply at all in this context of a ‘shield for a third party’. Point (i) is at best a dogmatic assertion.¹³¹

7.61 As for (2), the second problem, the *Scruttons* case (1962)¹³² increased the cost of insurance relating to carriage of goods by requiring double insurance: because the third party has no protection under an exclusion clause against liability, he would need to take out insurance against that liability. That insurance premium would increase freight charges. The effect of the *Scruttons* case was to transfer this insurance risk from A’s insurer to T. As the following discussion will show, the problem created by the *Scruttons* case can now be neatly countered by the 1999 Act (7.62) (a more

128 [1962] AC 446, 473, HL.

129 [1924] AC 522, HL; cf *London Drugs Ltd v. Kuehne & Nagel International Ltd* (1992) 97 DLR (4th) 261 (Supreme Court of Canada): third party benefited by exclusion clause; free-standing exception to privity doctrine.

130 [1962] AC 446, HL.

131 N. Andrews, (1988) 8 LS 12, 17–18 (no strength in the proposition that A and B should have a free hand to vary or terminate their contract; *Treitel* (12th edn, London, 2007), 14–017.

132 [1962] AC 446, HL.

convoluted evasion was achieved in the 1970s using common law devices: the *Himalaya* clause, 7.63).

- 7.62 *Exclusion clauses and the 1999 Act.* The Act allows the benefit of an exclusion clause to be conferred upon a third party by A and B in each of these important contexts: contracts for carriage of goods by air, sea, rail or road.¹³³
- 7.63 *The 'Himalaya' clause upheld in the New Zealand Shipping case.* The Privy Council in *New Zealand Shipping Co. Ltd v. AM Satterthwaite & Co. Ltd ('The Eurymedon')* (1975)¹³⁴ had found a means of circumventing the rule in the *Scruttons* case (1962).¹³⁵ The essence of the reasoning in the *New Zealand Shipping* case is that A and B can validly create a 'side contract' in favour of T, using a so-called '*Himalaya* clause',¹³⁶ thus creating *privity of contract between A and T*. Because A and T are now regarded as contracting parties, A being yoked to T, there is no direct conflict with the *Scruttons* case because that decision only prevents a *non-party* from taking the benefit of this 'shield'. Following the *New Zealand Shipping* case (1975),¹³⁷ T has lost the problematic status of a 'non-party' and has been 'bumped up' to the superior status of a 'full contractual party'.

In the *New Zealand* case (1975), A, the owner of goods (the consignor), had paid to have his goods shipped by B, the carrier (if title to the goods passes under a bill of lading, then A1, the consignor, is succeeded by A2, the consignee; A2 then stands in the shoes of A1 and is bound by the A/B and A/T contracts). In the contract of carriage between A and B, there was a cumbersome clause (the so-called '*Himalaya* clause'). This clause purported to create a shield in favour of third parties, such as firms of stevedores (companies responsible for loading and unloading ships). The clause provided:

[N]o servant or agent of the carrier (including every independent contractor from time to time employed by the carrier) shall in any circumstances whatsoever be under any liability whatsoever to the shipper, consignee or owner and every exception, limitation, condition and liberty herein contained ... shall also be available and shall extend to protect any such servant or agent ... and for the purpose of all the foregoing provisions ... the carrier is or shall be deemed to be acting as agent or trustee on behalf of and for the benefit of all persons who are or might be agents (etc. ...).

T's crane operator negligently dropped goods into the sea and they were damaged. T, the stevedore company, then raised the exemption clause as a defence (or 'shield') against the cargo-owner A's claim in the tort of negligence for damage to A's property. By a three to two majority, the Privy Council upheld this defence in favour of T. The majority's reasoning involved these steps:¹³⁸

133 On the special position of exclusion clauses, see sections 1(6) and 6(5) ('... except that ...').

134 [1975] AC 154, PC.

135 [1962] AC 446, HL.

136 *Adler v. Dickson ('The Himalaya')* [1954] 2 Lloyd's Rep 267; [1955] 1 QB 158.

137 [1975] AC 154, PC.

138 For Lord Goff's overview, see '*The Mahkutai*' [1996] AC 650, PC (for details of that case, see 7.65); other overviews are in '*The Starsin*' [2004] 1 AC 715, HL, at [34], [56], [57], [93], [146] to [153], [163] and [197] to [201].

- (1) B acts as T's agent by inserting a *Himalaya* clause into the A/B contract;¹³⁹ that clause is an offer made by A to T, which B, as T's agent, communicates to T.
- (2) There is no need for T to communicate to A acceptance of such a unilateral contract; T's performance of the condition is enough.
- (3) The contractual relation between A and T is a unilateral contract: that T should have the benefit of the exemption clause in return for his work in unloading B's ship (the exclusion clause will either exclude T's liability in negligence towards A, or cap it, or impose a time limit on A's liability towards T).
- (4) It does not matter that T, the stevedores, were already contractually obliged towards B to do this very same work; T provides consideration for A's promise by T's commencement of the job of unloading the ship.¹⁴⁰
- (5) The upshot of this is that the *Himalaya* clause creates privity of contract between A and T, and so T will no longer be a third party; there is no direct conflict with *Scruttons*, which bars only a *non-party* from taking the benefit of this 'shield'.
- (6) In *The New York Star* (1981), the sequel to the *New Zealand Shipping* case (1975), the Privy Council took the sensible further step and held that, if T has *already unloaded the ship*, and is storing A's goods in a warehouse, awaiting collection, the umbrella of the *Himalaya* clause continues to protect T.¹⁴¹

Lord Simon and Viscount Dilhorne dissented in the *New Zealand Shipping* case, objecting that the analysis of offer and acceptance had been quite artificially misapplied on these facts (under general 'offer and acceptance' principles (3.08), T can only accept the offer if T is aware of it).¹⁴² These dissents, however, seem misplaced. On the facts of the *New Zealand Shipping* case, it was not fanciful to impute to T awareness of the offer, since B and T worked closely together. But, in other cases, it must be admitted that it is artificial to impute awareness to T (although in *The New York Star* (1981) the Privy Council dismissed this objection as legal pedantry).¹⁴³

However, there are two important limits upon the operation of the *Himalaya* clause, and these will be examined in the next two paragraphs.

7.64 '*Himalaya*' clause ineffective if wrongdoer a maritime 'carrier' of goods. Does it matter that T is a 'carrier' (although not the primary carrier) of goods by sea? In '*The Starsin*' (2004), the House of Lords answered 'yes',¹⁴⁴ because an international maritime convention (the Hague-Visby Rules) provides that no 'maritime carrier' can exclude his liability.¹⁴⁵

139 '*The Mahkutai*' [1996] AC 650, PC: if B is unauthorised to be T's agent, T can later ratify B's purported agency.

140 Applying *Scotson v. Pegg* (1861) 30 LJ Ex 225.

141 [1981] 1 WLR 138, PC; noted by M. A. Clarke, [1981] CLJ 17; cf *Raymond Burke Motors Ltd v. Mersey Docks & Harbour Co.* [1986] 1 Lloyd's Rep 155 (T's negligence occurred *before* the contract of carriage began; cars in a parking 'lot' controlled by T).

142 See 3.08 on *Gibbons v. Proctor* and *R v. Clarke*.

143 [1981] 1 WLR 138, PC.

144 [2004] 1 AC 715, HL; noted by E. Peel, (2004) 120 LQR 11.

145 [2004] 1 AC 715, HL, at [32], noting Article III, Rule 8, of the Hague-Visby Rules (within Carriage of Goods by Sea Act 1971, Schedule).

In *'The Starsin'* (2004), B hired T's ship to transport A's goods from port X to port Y. During the voyage, the cargo was damaged because the hold of T's ship became wet. A, the owner of the goods, did not sue B for breach of contract because B had become insolvent. Instead, A sued T. And T attempted to raise an exclusion clause contained in A and B's contract in favour of T.

The House of Lords held that the Hague-Visby Rules invalidate an exclusion clause as between a cargo-owner and any 'carrier', including the ship's owner (note, however, that the Rules apply only where the exclusion clause purports to exclude or restrict the liability of a maritime 'carrier', as distinct from a stevedore or warehouseman).

- 7.65 *'Himalaya' clause ineffective in case of exclusive jurisdiction clauses.* The Privy Council in *'The Mahkutai'* (1996)¹⁴⁶ reveals another limit upon the operation of *Himalaya* clauses: the analysis used in the *New Zealand Shipping* case (1975)¹⁴⁷ cannot work for exclusive jurisdiction clauses. Lord Goff in *'The Mahkutai'* distinguished between the 'mutual' phenomenon of an exclusive jurisdiction clause (binding *both parties* to a nominated forum) and the unilateral protection conferred by an exclusion clause (limiting or excluding *one party's* liability for breach). Only in the case of an exclusion clause will a *Himalaya* clause confer the benefit of the clause on stevedores, etc.

An exclusive jurisdiction clause stipulates that legal disputes arising from the relevant job or transaction can only be litigated in a nominated jurisdiction (for example, 'in the courts of Singapore'). Such a jurisdiction clause normally binds all parties to the relevant transaction and it creates mutual restrictions and mutual rights, a set of matching shields: both parties are restricted to suing in Singapore. By contrast, an exclusion clause is a single shield protecting only T: A is not intended to have this shield, and so there is no mutuality as between A and T. And so Lord Goff in *'The Mahkutai'* (1996) drew a distinction between the 'mutual' phenomenon of an exclusive jurisdiction clause (binding both parties to a nominated forum) and the unilateral protection conferred by an exclusion clause (limiting or excluding one party's liability for breach).

- 7.66 *'The Mahkutai' decision and non-exclusive jurisdiction clauses.*¹⁴⁸ A non-exclusive jurisdiction clause empowers A and/or T to sue each other in a specified jurisdiction *in addition to* any other jurisdictions otherwise available independently of the jurisdiction clause. Such a clause has no restrictive element. Instead, it broadens by consent the available jurisdictions in which litigation can take place.¹⁴⁹ The Privy Council in *'The Mahkutai'* (1996)¹⁵⁰ did not consider this type of jurisdiction clause. If T were to sue A, relying on the combination of a *Himalaya* clause which purports to give T the benefit of a non-exclusive jurisdiction clause (whether a mutual clause or one operating solely in

146 [1996] AC 650, PC.

147 [1975] AC 154, PC.

148 A. Briggs, *Agreements on Jurisdiction and Choice of Law* (Oxford, 2008).

149 *Deutsche Bank AG v. Highland Crusader Offshore Partners LP* [2009] EWCA Civ 725; [2010] 1 WLR 1023, at [50], [64], [105] and [106].

150 [1996] AC 650, PC.

T's favour), it is arguable that the reasoning in *'The Mahkutai'* (1996) would not obstruct T. This is because such a non-exclusive clause contains no restriction: on the contrary, its function is to expand the choice of fora available to A and T (this is even more obviously the case if the jurisdiction clause is a *non-mutual* non-exclusive jurisdiction clause intended solely to benefit T).

8. PRIVACY OF CONTRACT AND 'BURDENS'

- 7.67 *General principle.* Contracts cannot be thrust on parties behind their backs. Freedom of contract (1.08), a cornerstone of private law, prevents Z ('Z' will denote the third party throughout section 8 of this chapter) from being burdened without his consent. And so X and Y cannot render Z liable for failure to act for the benefit of X or Y.
- 7.68 However, there are four exceptions to (perhaps better regarded as qualifications upon) this notion that Z cannot be affected detrimentally by the contractual relations between X and Y. These are: (1) the torts of inducing breach of contract and interference by unlawful means with a contract; (2) restrictive covenants affecting freehold land; (3) injunctions to prevent knowing interference with contractual rights affecting other types of property, especially goods; (4) the doctrine of 'bailment on terms'. These are considered in turn.
- 7.69 *Procurement of a breach of contract and unlawful interference with another's contract.* The scope of this branch of tort law is now governed by *OBG Ltd v. Allan* (2008)¹⁵¹ where the House of Lords maintained the distinction between (1) the tort of *inducing a breach of contract* and (2) the tort of *interfering by unlawful means with a contract*.
- 7.70 The tort of *inducing a breach of contract* is traceable to *Lumley v. Gye* (1853).¹⁵² Unlawful means are not required. The central question is whether Z has intentionally induced another to breach a contract (for example, Z persuades Y to leave his manager, X; and this constitutes a breach of contract by Y *vis-à-vis* X). Z will be liable in tort towards X, the victim of Y's breach of contract. As Lord Hoffmann explained in the *OBG* case (2008):¹⁵³

To be liable for inducing breach of contract, you must know that you are inducing a breach of contract. It is not enough that you know that you are procuring an act which, as a matter of law or construction of the contract, is a breach. You must actually realise that it will have this effect ... If someone knowingly causes a breach of contract, it does not normally matter that it is the means by which he intends to achieve some further end or even that he would rather have been able to achieve that end without causing a breach ... On the other hand, if the breach of contract is neither

151 *OBG Ltd v. Allan* [2007] UKHL 21; [2008] 1 AC 1.

152 (1853) 2 E & B 216; G. H. L. Fridman, 'Lumley v. Gye and the (Over?)Protection of Contracts', in J. W. Neyers, R. Bronaugh and S. G. A. Pitel (eds.), *Exploring Contract Law* (Oxford, 2009), 225 ff.

153 [2007] UKHL 21; [2008] 1 AC 1, at [39], [42] and [43].

an end in itself nor a means to an end, but merely a foreseeable consequence, then ... it cannot for this purpose be said to have been intended.

- 7.71 As for the tort of *interference with another's contract by unlawful means*, Lord Hoffmann explained in the *OBG* case (2008):¹⁵⁴

Unlawful means [are] acts intended to cause loss to the claimant by interfering with the freedom of a third party in a way which is unlawful as against that third party and which is intended to cause loss to the claimant. [This tort] does not in my opinion include acts which may be unlawful against a third party but which do not affect his freedom to deal with the claimant.

- 7.72 *Restrictive covenants affecting land*. Z, a purchaser of land can become subject to a restrictive covenant originally agreed between X and Y (for example, an undertaking by Y and his successors in title that they will not use the relevant premises as a public house for the consumption of alcohol). The doctrine of restrictive covenants affecting freehold property is an established aspect of land law, traceable to *Tulk v. Moxhay* (1848).¹⁵⁵ Y's successors are bound regardless of their knowledge of the covenant. However, restrictive covenants cannot impose positive duties to act.

- 7.73 *Injunction to prevent knowing interference with contractual rights concerning other types of property, especially goods*. In some circumstances, X or Y can obtain an injunction against Z if Z has acquired rights in relevant property (tangible movable property, or intangible property such as a fund) *knowing* that X and Y have a subsisting contract (for example, a contract of hire) affecting that property and Z's proposed conduct will interfere with Y's performance of the contract. The injunction cannot, however, positively compel Z to act or to pay.¹⁵⁶ Browne-Wilkinson J in *Swiss Bank Corporation v. Lloyds Bank Ltd* (1979)¹⁵⁷ surveyed the long line of cases.

- 7.74 *Bailment of goods 'on terms'*. Z, an owner of goods, having given possession of those goods to a bailee (Y) (see 7.75 on the nature of bailment), can become subject to an exclusion clause (or jurisdiction clause) in a contract of sub-bailment between X (a sub-bailee) and Y, provided Z implicitly consented to that sub-bailment by Y to X. The 1999 Act (7.34) does not affect this situation because it is concerned only with the conferring on third parties of the *benefit of rights and not with the imposition upon third parties of burdensome aspects of contracts*. Before considering this topic further, it is necessary to summarise the nature of bailment.

¹⁵⁴ *Ibid.*, at [51].

¹⁵⁵ (1848) 2 Ph 774.

¹⁵⁶ *Law Debenture Trust Corporation v. Ural Caspian Oil Corporation Ltd* [1983] 1 WLR 138, 144, *per* Hoffmann J; noted by A. Tettenborn, [1983] CLJ 382 (appeal on a different point, [1995] Ch 152, CA; noted by P. Cane, (1995) 111 LQR 400).

¹⁵⁷ [1979] Ch 548, 575 (unaffected by final appeal, [1982] AC 584, HL); Browne-Wilkinson J considered these authorities: *De Mattos v. Gibson* (1858) 4 De G & J 276; *Manchester Ship Canal Co. v. Manchester Racecourse Co.* [1901] 2 Ch 37; *The Strathcona* [1926] AC 108, PC; *Port Line Ltd v. Ben Line Steamers Ltd* [1958] 2 QB 146, Diplock J.

7.75 *Nature of bailment.* Bailment is a possessor's (a *bailee's*) responsibility for goods owned by the *bailor* (or, short of ownership, the bailor might have a right to possession). The bailee assumes responsibility to exercise reasonable care of the owner's goods. This relation normally involves a contract between the bailor and the bailee, but a contract is not necessary. Bailment requires possession to be taken by the bailee. The transitory control exercised by the stevedores in the *New Zealand Shipping* case (1975)¹⁵⁸ (7.63) did not involve a relation of bailment. But taking goods into possession, once unloaded, can involve a relation of bailment. Furthermore, the bailee, Y, can sub-bail Z's goods to another, X. This commonly happens when goods are transported, possession passing through several successive pairs of hands.

7.76 If there is an exclusion clause (chapter 15) or an exclusive jurisdiction clause (7.65) in the X/Y sub-contract, is Z *subject* to it (that is, 'burdened' by it, even though a non-party)? The Privy Council's decision in *The Pioneer Container* (1994)¹⁵⁹ said that Z would be subject in this way, but *only if* Z consents expressly or impliedly to Y's sub-bailing of the goods to X (approving Lord Denning MR's statement in *Morris v. CW Martin & Sons Ltd* (1966)¹⁶⁰ that 'the owner is bound by the conditions if he has expressly or impliedly consented to the bailee making a sub-bailment containing those conditions').

In *The Pioneer Container* (1994),¹⁶¹ Z, the owner, bailed his goods to Y, a carrier, and Z expressly authorised Y to sub-bail the goods. Y used X, a ship-owner, to transport the goods. The contract between X and Y contained an exclusive jurisdiction clause, nominating Taiwan as the sole forum for litigating disputes concerning the X/Y carriage contract. X's ship sank in fog and Z's cargo was lost. Z sued X for damages in Hong Kong. X successfully invoked as against Z the exclusive jurisdiction clause. X thus obtained a stay of Z's Hong Kong proceedings.

As for exclusive jurisdiction clauses (as on the facts of *The Pioneer Container* (1994)),¹⁶² the result is that both Z's action against X and any possible action between X and Y will be channelled to the same forum (on the facts, to Taiwan, nominated as the exclusive jurisdiction). This renders resolution of disputes predictable and convenient. As for exclusion clauses, the same result will also make commercial sense, for if this clause is ineffective to protect him, Z will need to increase his insurance cover. This extra cost will be 'passed up the chain' by X to Y (on this commercial factor, see 7.61).

158 [1975] AC 154, PC.

159 [1994] 2 AC 324, PC; noted by A. Tettenborn, [1994] CLJ 440.

160 [1966] 1 QB 716, 729, CA (the Privy Council in '*The Pioneer Container*' [1994] 2 AC 324, disapproved Donaldson J's *obiter* view in *Johnson Matthey & Co. v. Constantine Terminals Ltd* [1976] 2 Lloyd's Rep 215, 222, that no such consent is required).

161 [1994] 2 AC 324, PC.

162 *Ibid.*

Chapter contents

1. Introduction *para. 8.01*
2. Effects of assignment *para. 8.02*
3. No assignment of duties *para. 8.03*
4. Modes of assignment *para. 8.04*
5. Extent of the assigned right *para. 8.07*
6. Non-assignable rights *para. 8.10*
7. Assignment distinguished from other doctrines *para. 8.12*

8

Assignment

1. INTRODUCTION¹

8.01 Summary of main points

- (1) The holder of certain contractual rights (the promisee and assignor, B) can transfer the right to a third party (the assignee, C) without the promisor's (A's) consent. Thus, where A owes B a debt or other chose in action,² the right-holder, B, can assign the benefit of this right to C.
- (2) In the case of a statutory assignment,³ the assignment by B to C must be in writing, and B or C must notify A of the assignment.
- (3) Such notice is also desirable in the case of equitable assignments.
- (4) Certain rights are intrinsically incapable of being assigned because they are personal to the A/B relationship.
- (5) A can preclude an assignment by inserting a prohibitory clause in his contract with B.

¹ Main sources: *Anson's Law of Contract* (29th edn, Oxford, 2010), chapter 22; A. P. Bell, *Modern Law of Personal Property* (London, 1989), chapter 15; *Chitty on Contracts* (30th edn, London, 2008), chapter 19; *Meagher, Gummow and Lehane's Equity: Doctrines and Remedies* (4th edn, Sydney, 2003), chapters 6 and 7; *Treitel* (12th edn, London, 2007), chapter 15; G. Tolhurst, *The Assignment of Contractual Rights* (Oxford, 2006); and M. Smith, *The Law of Assignment* (Oxford, 2007). Tolhurst, at 1.01 n. 2, and Smith, at lxxi ff, provide large bibliographies. See also A. M. Tettenborn, 'Assignments, Trusts, Property, and Obligations', in J. W. Neyers, R. Bronaugh and S. G. A. Pitel (eds.), *Exploring Contract Law* (Oxford, 2009), 267 ff; A. M. Tettenborn, 'Problems in Assignment Law', in A. Burrows and E. Peel (eds.), *Contract Formation and Parties* (Oxford, 2010); and C. H. Tham, 'The Nature of Equitable Assignment and Anti-Assignment Clauses', in J. W. Neyers, R. Bronaugh and S. G. A. Pitel (eds.), *Exploring Contract Law* (Oxford, 2009), 283 ff.

² For classification of choses in action, see M. Smith, *The Law of Assignment* (Oxford, 2007), chapters 2 and 3.

³ Section 136 of the Law of Property Act 1925.

M. Smith, *The Law of Assignment* (Oxford, 2007)

2. EFFECTS OF ASSIGNMENT

8.02 Assignment has four effects (here, A is the promisor, B is the promisee, and C is the assignee):

- (1) A, once notified, is obliged to pay C.
- (2) To enforce the obligation created by the assignment in C's favour, C can sue A directly, without joining B as a party to the claim. This is true of statutory assignment (8.04) and of equitable assignment (8.05) of equitable choses in action. In the case of equitable assignment of a legal chose in action, such as a debt, the assignee must join the assignor as party to the claim (although there might be exceptions, where such joinder becomes unnecessary or it has been waived).⁴
- (3) A's obligation to B is discharged if, pursuant to a valid assignment by B to C, A pays C in full.
- (4) By contrast, if, after B's assignment of the right to C, A instead pays B, this payment is ineffective to discharge A's newly transferred obligation towards C.

3. NO ASSIGNMENT OF DUTIES

8.03 *Vicarious performance contrasted.* A promisor cannot assign the 'burden' of his obligation to another. Only rights can be assigned, and not duties. Thus, one cannot, without the promisee's consent (that is, the party entitled to contractual performance), transfer the burden of a contract from one promisor to a new party. The explanation for this is that the principle of 'freedom of contract' (1.08) gives the promisee the right to choose 'who the promisor will be', that is, he can decide who will owe him a contractual duty. But there are situations where a party, Z, cannot complain if another, X, in fact performs an outstanding contractual duty owed by Y to Z. This possibility is known as 'vicarious performance' (by X on Y's behalf, for Z's benefit).⁵ Technically, vicarious performance is consistent with the principle, stated above, that duties cannot be transferred without the consent of the person who holds the relevant right. The reason why there is no inconsistency is that, where vicarious performance occurs, the duty is not transferred. In fact, the original contractual obligation between Y and Z remains intact. A legal change occurs only because Y's obligation to Z is discharged by X's performance. In this situation, X's performance was requested by Y. In effect, Y has sub-contracted his task to X, who has then performed satisfactorily.

4 *Chitty on Contracts* (30th edn, London, 2008), 19-038 and 19-039.

5 M. Smith, *The Law of Assignment* (Oxford, 2007), 4.82 ff.

Thus it might be possible under a contract between Y and Z for Y to sub-contract performance to a third party, X. X does not have this burden thrust upon him: he has assented with Y to perform the job. Nor does Z lose his contractual rights against Y. Thus, if X performs satisfactorily, Y's duty to Z is discharged; but, if X performs badly, Y will be in breach of his contract; and X might also be in breach of a tortious duty of care towards Z. Nor can Z legitimately complain that the job has been done by X and not by Y. Such an objection would be valid only if Y's personal identity were crucial to the transaction (contrast the case, for example, where University Z has hired Professor Y to give lectures for a term, but Y, without Z's permission, sub-contracts to X, a young scholar of less renown; unknown to Z, X gives the lectures instead of Y). However, the assumption for the moment is that Y's identity was not crucial: a reasonable person in Z's position would not object to such sub-contracting by Y to X.

4. MODES OF ASSIGNMENT⁶

- 8.04 *Statutory assignment.*⁷ The requirements for assignment of a debt or other chose in action under section 136(1) of the Law of Property Act 1925 are as follows. First, B must assign *in writing* the right to C, that is, B must notify C, and effect the transfer of the contractual right, in written form; B must sign this document; there is no need for C to provide consideration for this transfer. Secondly, there must be written notice to A of the assignment (notice can be given by B or C). The 1925 Act provides that the assignment takes effect 'from the date of such notice'. Thirdly, the assignment must be 'absolute'. This means that A's duty to pay C should not be dependent on A discovering the balance of entitlement between B and C (for example, where B purports to assign so much of A's debt as is necessary to satisfy outstanding obligations owed by B to C; in this situation, the objection is that A cannot readily discover whether he stills owes money to C, the assignee, because that question depends on the state of accounts between B and C).⁸ Fourthly, there are restrictions on what can be assigned under this statute: (1) one cannot assign part of the debt owed by A to B (but, if B assigns the unpaid balance of A's debt, the assignment can be a valid statutory assignment because B has transferred all that remains of A's debt, and in this sense this is not a partial assignment of A's debt); (2) nor can there be a statutory assignment by way of charge upon a fund or account owed by A to B; finally, (3) the right assigned must either be an existing obligation or a right which will arise under a contract which is already operative; there cannot be a statutory assignment of a wholly prospective right.⁹

⁶ *Ibid.*, at chapters 5–7.

⁷ *Treitel* (12th edn, London, 2007), 15-010 ff; and M. Smith, *The Law of Assignment* (Oxford, 2007), chapter 10, for exposition of section 136(1) of the Law of Property Act 1925 (formerly section 25(6) of the Judicature Act 1873).

⁸ *Treitel* (12th edn, London, 2007), 15-012, explaining case law on this point.

⁹ *Ibid.*, at 15-025.

8.05 *Equitable assignment.*

- (1) *Nature.* If, for some reason, an attempted statutory assignment fails, a valid equitable assignment might nevertheless occur. An equitable assignment is effective even though notice is not given to A, the debtor (contrast statutory assignment where such notice must be given to A). Nevertheless, notice to A in the case of equitable assignment is highly desirable for two reasons: first, because A is then required to pay C directly (A's payment to B, after notice of the assignment, does not discharge A's liability to pay the assignee); secondly, notice determines priority as between successive assignees. If the right assigned is a legal debt or obligation (as opposed to a purely equitable right, for example a right arising by trust or entitlement to a legacy), equitable assignment requires C to join B in any litigation to enforce A's duty. Furthermore, writing is required where the equitable assignment concerns a disposition of a subsisting equitable interest.¹⁰ Subject to that, equitable assignment can be oral (by notification of the transfer to the assignee).
- (2) *Equitable assignment can be gratuitous.* There is no need for 'consideration' (on which generally see chapter 5) in the case of a perfected equitable assignment of an equitable right (although here writing is required: see above). As for gratuitous equitable assignment of a legal chose in action, the better view is that a perfected assignment in equity can be valid even though there is no consideration and despite non-compliance with the statutory mode of assignment.¹¹
- (3) *Equitable assignment of a wholly prospective right.* This can take effect as an agreement to assign, but this will require C to have provided consideration to B.

8.06 *Specific statutory contexts.* Assignments of patents and copyright and various other special types of right are subject to specific rules.¹²

5. EXTENT OF THE ASSIGNED RIGHT

8.07 C's claim as assignee can be defeated if A, the main debtor, has a right as against B to rescind the relevant obligation on the basis of B's misrepresentation, non-disclosure or fraud, etc. Thus, C cannot receive as assignee a right or an interest greater than that (purportedly) transferred. For example, if B's 'right' is in fact void for mistake or illegality, C cannot be placed in any superior position *vis-à-vis* A. This limitation is expressed by saying that C's assigned rights are subject to any 'equities' pertaining as between A and B.¹³

¹⁰ Section 53(1)(c) of the Law of Property Act 1925.

¹¹ As *Treitel* (12th edn, London, 2007), 15-035, attractively contends.

¹² *Chitty on Contracts* (30th edn, London, 2008), 19-003, citing (among other contexts) sections 30 and 33 of the Patents Act 1977 and sections 90 and 94 of the Copyright, Designs and Patents Act 1988; and *Anson's Law of Contract* (29th edn, Oxford, 2010), 663.

¹³ *Chitty on Contracts* (30th edn, London, 2008), 19-070 ff.

8.08 Furthermore, C's rights against A are also subject to any right of set-off which A has against B arising out of the transaction between A and B. However, if the right of set-off is personal to B, C will not be subject to it, at any rate if the set-off has arisen after notice of assignment to A.¹⁴ If A pays money to C, a valid assignee, but this money was not owing by A to B, so that A has 'overpaid', A cannot recover this payment from C if the contract between A and B provided expressly for adjustment of overpayments directly as between A and B. And A's inability to obtain repayment from the assignee C extends to the situation where B cannot repay A because B has become insolvent:

*In Pan Ocean Shipping Ltd v. Creditcorp Ltd ('The Trident Beauty') (1994),*¹⁵ a charterparty between A, the charterer, and B, the owner, entitled B to recover hire from A. B assigned to C these rights to hire. The right assigned was for payment in advance of each period of hire. A paid C, in accordance with this assignment. C's receipt from A of hire covered the period when the vessel was in fact 'off-hire'. A surviving contractual clause between A and B provided that B would repay or make allowance for any over-payment. B had become impecunious. The House of Lords held that A could not recover payment from the assignee.

8.09 *The assignee can recover damages no less extensive than those to which the assignor would have been entitled if the assignment had not taken place. Offer-Hoar v. Larkstore Ltd (2006)*¹⁶ acknowledges that, following an assignment of a cause of action by a former land-owner to the present owner, the assignee can recover damages no less extensive than those to which, B, the assignor would have been entitled if the assignment had not taken place. However, the assignee cannot augment the liability by bringing to the quantification of the claim factors peculiar to the assignee.¹⁷

In Offer-Hoar v. Larkstore Ltd (2006), the facts were as follows. In 1998, A, the promisor, had made a soil report on a site for B, the eventual assignee. The report contained no clause prohibiting assignment. In 1999, B transferred the site to C, a developer. In 2001, damage occurred when there was a landslide on this site. A's failure in its report to alert B to this danger was a breach of contract. In 2004, B assigned to C the benefit of B's cause of action in respect of A's breach of contract.

The Court of Appeal held that A could not defeat C's claim by saying that the value of C's assignment rights was capped by the amount of loss suffered by B. The rights assigned included the right to compensation in respect of losses as they might unfold from the time the breach of contract had occurred. That liability might emerge after the transfer of the site

¹⁴ *Anson's Law of Contract* (29th edn, Oxford, 2010), 669–70.

¹⁵ [1994] 1 WLR 161, HL.

¹⁶ [2006] EWCA 1079; [2006] 1 WLR 2926; *Treitel* (12th edn, London, 2007), 14-045; applied in *Landfast (Anglia) Ltd v. Cameron Taylor One Ltd* [2008] EWHC 343 (TCC), Akenhead J.

¹⁷ *Dawson v. Great Northern and City Railway Co.* [1905] 1 KB 260, CA (considered in the present decision [2006] EWCA 1079; [2006] 1 WLR 2926, at [38], [48], [78] and [87]).

and either after or before (as on these facts) the assignment. Of course, the decision does not affect any defences A might have as against C based on the rules of limitation of action, causation, remoteness of damage, etc.

Rix LJ¹⁸ linked this aspect of the law concerning assignment with the parallel development of rights by a promisee to sue in respect of loss eventually suffered by a third party transferee of chattels or land, or a third party owner of land who has financed a building contract between A and B affecting that owner's land (on that development, see 7.25 ff). He noted that, in both contexts, the modern law strives to ensure that the party in contractual default is made to pay compensation for the loss which has in fact been suffered. Indeed, had there not been an assignment in this case, a claim by B on behalf of C might have provided a different route to enabling C to receive compensation. But B's assignment to C showed on these facts that B wished to have no part in any such litigation.

6. NON-ASSIGNABLE RIGHTS¹⁹

8.10 The initial agreement between A and B can validly prohibit such a transfer.²⁰ There are also bars against assignment based on statute or public policy.²¹ However, assignments can be valid even though the purpose of the arrangement involved an element of legal evasion, notably: (1) assignment by B to C so that C can bankrupt A, the debtor;²² or (2) assignment by B, a company, to C, an individual, so that C (unlike B) will not be vulnerable to an application for security for costs;²³ or (3) assignment by B, a company, to C, an individual, so that C (unlike B) can seek legal aid in respect of the underlying claim.²⁴

8.11 Certain rights of action are not assignable:

- (1) most tort actions;²⁵
- (2) unliquidated claims for contractual damages unless C, the purported assignee, has a 'genuine commercial interest' in taking the assignment (for example, C has made a loan to B, the assignor, and is now seeking to recoup some of this by receiving assigned rights as against A);²⁶ or C, the assignee, has received a proprietary interest and the relevant claim relates to that interest;²⁷

18 [2006] EWCA 1079; [2006] 1 WLR 2926, at [80] to [87].

19 M. Smith, *The Law of Assignment* (Oxford, 2007), chapter 12.

20 *Linden Gardens Trust Ltd v. Lenesta Sludge Disposals Ltd* [1994] 1 AC 85, HL; *Treitel* (12th edn, London, 2007), 15-050; M. Smith, *The Law of Assignment* (Oxford, 2007), 12.124 ff.

21 *Treitel* (12th edn, London, 2007), 15-066 ff; M. Smith, *The Law of Assignment* (Oxford, 2007), 12.49 ff.

22 *Fitzroy v. Cave* [1905] 2 KB 364, CA.

23 *Norglen Ltd v. Reed Rains Provincial Ltd* [1999] 2 AC 1, HL.

24 Consolidated appeal in the *Norglen* case, *ibid.*

25 *Treitel* (12th edn, London, 2007), 15-060, contending that this category should not be applied uncritically.

26 *Trendtex Trading Ltd v. Crédit Suisse* [1982] AC 679, HL; *Treitel* (12th edn, London, 2007), 15-065.

27 *Ibid.*, at 15-064.

- (3) a right to rescind a transaction (for example, by reason of undue influence) is not assignable;²⁸ but one can validly assign a right to seek compensation for breach of contract or a debt;
- (4) certain personal undertakings are not transferable. For example, the benefit held by a publisher of an author's agreement to publish a book with that publishing house is not assignable by the publisher to another. Another example is a motor insurance policy, because the identity of the relevant driver is bound, or likely, to involve personal attributes peculiar to that driver. Therefore, the named driver cannot assign the insurance cover to another.²⁹

7. ASSIGNMENT DISTINGUISHED FROM OTHER DOCTRINES

8.12 Assignment is the transfer of a contractual right. It can be distinguished from the following:

- (1) *Novation*.³⁰ This involves extinction of one contract (the A/B contract) and replacement by another (the A/C contract): see Lord Selborne's statement in *Scarf v. Jardine* (1882),³¹ distinguishing novation of A/B contract No. 1 by A/B contract No. 2, and the novation of a contract between A and B by the creation of a contract between A and C, where C is a new party. In the latter case, novation involves A's duty to B being extinguished and a fresh contract arising between A and C. This is not the same mechanism, therefore, as a transfer, by assignment, from B to C of B's right against A.
- (2) *Third party beneficiary rights*. If A promises B to confer a benefit on T, the latter can acquire a direct right of action under the Contracts (Rights of Third Parties) Act 1999 (7.34 ff). T is then designated a third party beneficiary from the inception of the relevant contract between A and B (those parties might retain powers of variation under the 1999 Act, until C has relied on the A/B undertaking, or C has communicated to A his wish to take advantage of that undertaking). The fact that T acquires a right under the original agreement contrasts with assignment, which is the transfer, subsequent to the contract's formation, of a right from the initial right-holder, B, to a new right-holder, C, the assignee.
- (3) *Negotiable instruments*. These are transferable by delivery, or by delivery and endorsement. The new holder acquires a direct right against the debtor without the need for notice to the debtor. The right acquired can be superior to the transferor's.³²

28 *Ibid.*, at 15-006, noting *Investors Compensation Scheme Ltd v. West Bromwich Building Society* [1998] 1 WLR 896, HL.

29 *Treitel* (12th edn, London, 2007), 15-051 ff, citing, notably, *Tolhurst v. Associated Portland Cement Manufacturers* [1902] 2 KB 660, 668, CA; see also *Jenkins v. Young Bros Transport Ltd* [2006] EWHC 151 (QB); [2006] 1 WLR 3189, at [12].

30 *Treitel* (12th edn, London, 2007), 15-003.

31 (1882) LR 7 App Cas 345, 351, HL.

32 *Chitty on Contracts* (30th edn, London, 2008), 19-085; *Treitel* (12th edn, London, 2007), 15-046 ff; *Anson's Law of Contract* (29th edn, Oxford, 2010), 677 ff.

- (4) *Revocable mandate.* B might authorise A to pay C. A's payment (in full) to C will then discharge A's obligation to B. C is normally capable of retaining the money against both A and B. Even while the mandate is operative, C acquires no direct right of action against A.³³ The mandate is revocable by B's notification to A.

³³ *Treitel* (12th edn, London, 2007), 15-018.

V

Vitiating elements

Chapter contents

1. Introduction *para. 9.01*
2. Nature of a 'misrepresentation' *para. 9.02*
3. Statements becoming either terms or 'collateral warranties' *para. 9.05*
4. Differences between compensation under the Misrepresentation Act 1967 (or in tort) and for breach of contract *para. 9.11*
5. Compensation in the tort of deceit *para. 9.12*
6. Damages under section 2(1) of the Misrepresentation Act 1967 *para. 9.14*
7. Rescission *ab initio* *para. 9.18*
8. Termination for breach and rescission for misrepresentation contrasted *para. 9.22*
9. Exclusion clauses and the Misrepresentation Act 1967 *para. 9.26*
10. Duties to disclose *para. 9.34*

9

Misrepresentation

1. INTRODUCTION¹

9.01 Summary of main points

- (1) A 'misrepresentation' is an inaccurate statement of fact which induces the other party to enter into the contract.
- (2) The two remedies applicable to misrepresentations are damages and the mutual dismantling of the parties' benefits received under the contract (known as 'rescission *ab initio*').
- (3) Damages are available as of right only if (a) the misrepresentation is fraudulent (the tort of deceit, 9.12),² or (b) the misrepresentation is negligent at common law (the tort of negligent misstatement, 9.15), or (c) the representor is liable under section 2(1) of the Misrepresentation Act 1967, a statutory tort (9.14). These heads of liability will be explained more fully below. For a convenient summary of the development of this topic, see Rix J's remarks in *Avon Insurance plc v. Swire Fraser Ltd* (2000).³
- (4) Currently, the 1967 Act's 'tort' is the representee's favoured source of compensation because the damages awarded are equivalent to those available under (3)(a) above, and

¹ J. Cartwright, *Misrepresentation, Mistake and Non-Disclosure* (2nd edn, London, 2007); D. O'Sullivan, S. Elliott and R. Zakrzewski, *The Law of Rescission* (Oxford, 2008), chapter 4; *Spencer Bower, Turner and Handley's Actionable Misrepresentation* (4th edn, London, 2000); A. Tettenborn (with D. Wilby and D. Bennett), *The Law of Damages* (London, 2003), chapter 17; for academic discussion, see S. J. Stoljar, *Mistake and Misrepresentation* (London, 1968), chapters 6 ff; P. S. Atiyah and G. H. Treitel, 'Misrepresentation Act 1967' (1967) 30 MLR 369; Law Reform Committee, *Innocent Misrepresentation* (Law Reform Committee, 10th Report, Cmnd 1782, 1962); cf New Zealand, *Misrepresentations and Breach of Contract* (Report of the Contracts and Commercial Law Reform Committee, Wellington, 1967; reprinted 1978), 9.4.1. On the nineteenth-century history of this topic, see M. Lobban, in W. Cornish, J. S. Anderson, R. Cocks, M. Lobban, P. Polden and K. Smith, *The Oxford History of the Laws of England*, vol. XII, 1820–1914: *Private Law* (Oxford, 2010), 409 ff.

² *Derry v. Peck* (1889) 14 App Cas 337, HL; on damages for deceit, see 9.12.

³ [2000] 1 All ER (Comm) 573; [2000] Lloyd's Rep IR 535, at [19] and [20].

because, once the claimant shows that the statement is false, the burden of proof rests on the representor to show he had reasonable grounds for making the statement.

- (5) Even if the misrepresentation is not culpable in any of these ways, the court has a discretion to award damages instead of allowing the contract to be rescinded (section 2(2) of the 1967 Act, cited at 9.21). However, this discretion does not apply if the statement was fraudulent.
- (6) Rescission is subject to the following four general equitable 'bars', any of which will be sufficient to preclude rescission: (a) inability to restore the parties in a practical sense to the pre-contractual position ('*restitutio in integrum* impossible'); (b) the subject matter of the contract between A and B has been acquired in good faith by a sub-purchaser; (c) affirmation of the contract by the representee; or (d) lapse of time rendering it unjust for the contract to be dismantled by rescission.
- (7) A misrepresentation can lead a double life: according to section 1(a) of the Misrepresentation Act 1967, even if (as occasionally occurs) a misrepresentation becomes a term of the eventual contract, it can simultaneously subsist as a misrepresentation.
- (8) It should also be noted that misrepresentation cannot be divorced from questions of 'mistake': all instances of misrepresentation involve the inducing of an error or misapprehension in the representee (see chapter 10 (on mistake) for types of error not attributable to a misrepresentation).
- (9) As for duties to disclose, the general proposition is that English law does not require a prospective party to point out to the other an imminent and ordinary bargaining mistake. Nor is there a general positive duty for a prospective party to reveal information which might be relevant to the transaction or to the fixing of its terms. However, a person cannot take unfair advantage of the other's confusion concerning the supposed terms of the agreement; and in specific situations, notably contracts of insurance, the law imposes a positive duty to reveal relevant information.

Law Reform Committee, *Precursor to the 1967 Act: 'Innocent Misrepresentation'* (Law Reform Committee, Tenth Report, Cmnd 1782, 1962)

R. Hooley (Case Note), 'Conundrum of Section 2(1) of the 1967 Act' (1991) 107 LQR 547

E. Peel (Case Note), 'Non-Reliance' Clauses and Section 3 of the 1967 Act' (2001) 117 LQR 545

2. NATURE OF A 'MISREPRESENTATION'

- 9.02 The essence of a misrepresentation is a false statement made by one person, even if he does not know that it is false, and even if he is not negligent in having made the

statement. Unless the statement is fraudulent (when inducement is presumed: see 9.04 at (7) below), the statement must be influential to the extent that the person decides, as a result of being misled, to enter into the contract: that is, his decision to form the agreement is made in reliance on the other's false statement. Rescission can be granted for a wholly innocent misrepresentation, as Sir George Jessel MR explained in *Redgrave v. Hurd* (1881)⁴ (but some degree of culpability is necessary if damages are sought: see 9.01 at (3), below).

In *Redgrave v. Hurd* (1881), Sir George Jessel MR said:

As regards the rescission of a contract, there was no doubt a difference between the rules of Courts of Equity and the rules of Courts of Common Law – a difference which of course has now disappeared by the operation of the Judicature Acts 1873–5, which makes the rules of Equity prevail. According to the decisions of Courts of Equity it was not necessary, in order to set aside a contract obtained by material false representation, to prove that the party who obtained it knew at the time when the representation was made that it was false. It was put in two ways, either of which was sufficient. One way of putting the case was, 'A man is not to be allowed to get a benefit from a statement which he now admits to be false. He is not to be allowed to say, for the purpose of civil jurisdiction, that when he made it he did not know it to be false; he ought to have found that out before he made it.' The other way of putting it was this: 'Even assuming that moral fraud must be shewn in order to set aside a contract, you have it where a man, having obtained a beneficial contract by a statement which he now knows to be false, insists upon keeping that contract. To do so is a moral delinquency: no man ought to seek to take advantage of his own false statements.' The rule in Equity was settled, and it does not matter on which of the two grounds it was rested.

Broken down further, a misrepresentation consists of the following elements:

- (1) The representation must be either by words or by conduct.
- (2) The statement must concern a matter of past or present fact or 'law'.
- (3) The statement should not involve the assertion of a mere matter of opinion.
- (4) The statement must be unambiguous, and not a 'mere puff'.
- (5) It must also be 'material', that is, a comment which, objectively, is apt to influence a reasonable person.
- (6) It must be made before the main contract.
- (7) It must be made by the representor, who becomes a party to the contract; and it must be addressed (normally directly, sometimes indirectly) to the representee who also becomes a party to the contract.
- (8) The allegedly misleading statement must not be false in a trivial sense.
- (9) If only the representee understood it in a sense that would be false, the statement will be a misrepresentation only if the representee's interpretation was objectively reasonable.
- (10) The statement is normally false when made and remains so at all stages prior to formation of the contract (on the special situation where an initially accurate statement is falsified by supervening events, before the contract is formed, see 9.03).

⁴ (1881) 20 Ch D 1, 12–13, CA.

- (11) The representee must be (a) aware of the statement, and (b) decisively influenced by it (there is an exception to proposition (b) if the statement was made fraudulently).

These points will now be expanded.

(1) *The misrepresentation must be a statement by words or a representation by conduct.*⁵ Instances of representations by conduct are shown in the following cases.

In *Spice Girls Ltd v. Aprilia World Service BV* (2002),⁶ the Spice Girls entered into negotiations in February 1998 ostensibly as an intact and continuing entity, whereas one of the group, namely, Geri Halliwell, 'Ginger Spice', had already told the others that she would be leaving the band quite soon. In April 1998, the five singers participated in photo shoots. This activity and other connected representations suggested that the band was not about to change its membership in this way. A formal agreement was reached on 6 May 1998. Ginger Spice then left the band on 27 May 1998. The agreement provided for sponsorship of the group on a world tour, in return for the group endorsing and providing publicity to promote a motor-scooter. After the defection of Ginger Spice, the scooter promotion ceased to be commercially feasible. The Court of Appeal, upholding Arden J's decision at first instance, held that the representor, the managing company of the band, was liable for damages under section 2(1) of the 1967 Act (cited at 9.14) for loss resulting from this misrepresentation.

In *Gordon v. Selico* (1986),⁷ Goulding J held that a vendor's decision to cover up dry rot in a property in order to conceal this problem from prospective purchasers and their surveyors was a misrepresentation by conduct that the property did not suffer from dry rot.

(2) *The statement must concern a matter of past or present fact or 'law'.* The extension of liability for misrepresentation to include misstatements of law is quite recent. The Court of Appeal in *Brennan v. Bolt Burdon* (2004)⁸ approved this development, introduced at first instance,⁹ following developments in the law of restitution.¹⁰

(3) *The statement should not involve the assertion of a mere matter of opinion.* The leading case is *Smith v. Land and House Property Co.* (1884),¹¹ in which the Court of Appeal held that there had been a statement of fact, rather than a non-committal indication of opinion, on these facts.

⁵ Cf non-disclosure, 9.34.

⁶ [2002] EWCA Civ 15; [2002] EMLR 27; *Chitty on Contracts* (30th edn, London, 2008), 6-011, 6-015.

⁷ (1986) 278 EG 53, CA.

⁸ *Brennan v. Bolt Burdon* [2004] EWCA Civ 1017; [2005] QB 303; *Treitel* (12th edn, London, 2007), 8-022 ff; J. Cartwright, *Misrepresentation, Mistake and Non-Disclosure* (2nd edn, 2007), 3.20 ff.

⁹ In *Brennan v. Bolt Burdon* [2004] EWCA Civ 1017; [2005] QB 303, the Court of Appeal approved Judge Rex Tedd QC in *Pankhania v. Hackney London Borough Council* [2002] EWHC 2441 (Ch), at [58].

¹⁰ *Kleinwort Benson Ltd v. Lincoln City Council* [1999] 1 AC 153, HL (abolishing mistake of law bar to recovery of money paid by error).

¹¹ (1884) 28 Ch D 7, CA (considered in *IEE Fund SA v. Goldman Sachs International* [2007] EWCA Civ 811; [2007] 2 Lloyd's Rep 449, citing also *Hummingbird Motors Ltd v. Hobbs* [1986] RTR 276, CA, and *Sumitomo Bank Ltd v. BBL* [1997] 1 Lloyd's Rep 487, Langley J; and see *Dimmock v. Hallett* (1866) LR 2 Ch App 21).

The freehold of 'The Marine Hotel' at Walton-on-the-Naze was sold at auction to the plaintiff investment company. The particulars of the auction stated that the hotel was let for the remaining twenty-seven years at £4,000 a year to 'Mr Fleck', a 'most desirable' tenant. This impliedly indicated that the vendor had a real basis for making this statement. In fact, the vendor had glossed over the fact that Fleck had been slow in paying the last quarter's rent. The sale was completed in August, and Fleck became insolvent in September. The purchaser company then came to its senses and sought rescission of the sale for misrepresentation. The Court of Appeal held that there had been a misrepresentation on these facts, Bowen LJ explained:¹²

A statement of ... opinion is in a sense a statement of a fact, about the condition of the man's own mind, but only of an irrelevant fact, for it is of no consequence what the opinion is. But if the facts are not equally known to both sides, then a statement of opinion by the one who knows the facts best involves very often a statement of a material fact, for he impliedly states that he knows facts which justify his opinion ...

The vendors state that the property is let to a most desirable tenant, what does that mean? [This] ... amounts at least to an assertion that nothing has occurred in the relations between the landlords and the tenant which can be considered to make the tenant an unsatisfactory one. That is an assertion of a specific fact ... In my opinion a tenant who had paid his last quarter's rent by dribbles under pressure must be regarded as an undesirable tenant.

A statement by a professional person, such as a solicitor, tends to be taken to imply that the person is aware of the background and that he has read the relevant documentation.

In *Nottingham Patent Brick & Tile Co. Ltd v. Butler* (1886),¹³ the vendor's solicitor, in the vendor's presence, said that the land to be sold was not known by him to be subject to any restrictive covenants. In fact, the solicitor 'did not have a clue', because he had not checked the title deeds. The purchaser sought rescission when he discovered that there was a restrictive covenant, confining the usage of the property to a brickyard. The solicitor's statement was imputed to the vendor. The Court of Appeal held that, even if the solicitor had honestly believed this statement, he had impliedly indicated that he had a reasonable basis for this belief, whereas he had not read the relevant deeds. Lord Esher MR said:¹⁴

The defendant's solicitor ... allowed himself, in his zeal for his client, to make statements which were calculated to lead the other side to believe that he was stating facts within his own knowledge.

Lindley LJ said:¹⁵

The vendor's solicitor admitted that 'I did not tell [the representee] that I had not read those deeds ... The plaintiffs bought upon ... the faith of the defendant's solicitor knowing that there were no [restrictive covenants].

¹² (1884) 28 Ch D 7, 15–16, CA.

¹³ (1886) 16 QBD 778, 787, CA; see also *Brown v. Raphael* [1958] Ch 636, 644, 649, CA, *per* Lord Evershed MR and Romer LJ (as explained in *Economides v. Commercial Union Assurance Co. plc* [1998] QB 587, 595, 599, CA).

¹⁴ *Nottingham Patent Brick* case (1886) 16 QBD 778, 787–8, CA.

¹⁵ *Ibid.*, at 790.

But not every honest statement of opinion carries the implication that the maker of the statement impliedly has some factual support for the assertion. It might be clear from the relevant context that there is no reason for the representee to be influenced at all by the representor because the latter lacks experience, or is manifestly ignorant of the surrounding facts, or has made quite clear that he has no intention to make an actionable statement (see discussion below of the *IFE Fund SA* case).

As for lack of experience, the clearest example is *Bisset v. Wilkinson* (1927).¹⁶

The vendor, who owned some land in New Zealand (where sheep greatly outnumber the human population) said that the land to be sold would have a capacity to support 2,000 sheep, if the land were converted to a sheep-farm. The Privy Council held that this was not a statement of fact. In short, this was an uneducated 'guesstimate'. The representor had manifestly ventured a mere matter of opinion. There was no question of special knowledge because he was not himself a sheep-farmer and the land had not been used for this purpose before. And so it was clear to the representee that the vendor was making a guess and not relying on any knowledge, skill, experience or expert report from a third party source.

Similarly, in *Economides v. Commercial Union Assurance Co. plc* (1998),¹⁷ the Court of Appeal held that the notion of an implied statement of fact, connected with a statement of opinion (as illustrated by *Smith v. Land and House Property Co.* (1884), discussed above) should not be overstretched.

The 21-year-old owner of a flat had insured its contents. He estimated the value of his and his parents' goods. He later made an insurance claim in respect of the parents' loss of jewellery, following a burglary. But the insurer denied liability, on the basis that he had understated the contents' value. However, the Court of Appeal held that, in this context, it is enough that the private party had made an estimate in good faith. Simon Brown LJ said:¹⁸ 'If insurers wish to place upon their assured an obligation to carry out specific inquiries or otherwise take steps to provide objective justification for their valuations, they must spell out these requirements in the proposal form.'

Furthermore, information can be expressly provided on the basis that there is no accompanying verification, nor an assumption of responsibility to supply updated information.

The Court of Appeal in *IFE Fund SA v. Goldman Sachs* (2007)¹⁹ upheld Toulson J's decision that no misrepresentation arose when a merchant bank, acting in good faith and without any

16 [1927] AC 177, PC (note the Privy Council's mention of the trial judge's findings, [1927] AC 177, 183–4).

17 [1998] QB 587, CA; noted M. A. Clarke, [1998] CLJ 24 and, in a longer article, H. Bennett, (1998) 61 MLR 886–98.

18 [1998] QB 587, 599–600, CA.

19 [2007] EWCA Civ 811; [2007] 2 Lloyd's Rep 449.

assumption of responsibility, sent information to prospective (and sophisticated) purchasers of bonds. The bank qualified its provision of this information, stating explicitly that the bank was not assuming liability for inaccuracy. Furthermore, the bank emphasised that the information was not to be assumed to have been updated and did not constitute a representation by any person that the information would be updated. And so the bank was held not to have made any actionable misrepresentation.

(4) *The statement must be unambiguous, and not a 'mere puff'.*²⁰

(5) *The statement must be 'material' (that is, a comment which, objectively, is apt to influence a reasonable person).*²¹

(6) The statement must be made before the main contract.

(7) *It must be made by the representor, who becomes a party to the contract,*²² *and it must be addressed (normally directly, sometimes indirectly) to the representee who also becomes a party to the contract.*²³ In the case of an action in deceit, it appears that the representor must have intended the information to be passed by X to the defendant and acted upon detrimentally: Wood V-C in *Barry v. Croskey* (1861),²⁴ approved by the House of Lords in *Peek v. Gurney* (1873),²⁵ and by the Court of Appeal in *Andrews v. Mockford* (1896).²⁶ In the case of a negligent misstatement, the test determining liability for such 'sideways' communication is whether it was reasonably foreseeable that the eventual and indirect representee would rely upon the representation.²⁷ In the case of a wholly innocent misrepresentation, the test is not clear, but Cartwright suggests²⁸ 'that the representor ... realised that his statement would be received by the [indirect] representee and that he might therefore act on it'.

(8) *Having regard to the whole mass of pre-contractual information supplied by the representor, the allegedly misleading statement must not be false in a trivial sense.* As Rix J said in *Avon Insurance plc v. Swire Fraser Ltd* (2000):²⁹

[A] representation may be true without being entirely correct, provided it is substantially correct and the difference between what is represented and what is actually correct would not have been likely to induce a reasonable person in the position of the claimants to enter into the contracts.

20 *Dimmock v. Hallett* (1866) LR 2 Ch App 21 (sale of land at auction; assurance that land 'fertile and improvable' a mere puff).

21 *Chitty on Contracts* (30th edn, London, 2008), 6-036, 6-037; *Museprime Properties Ltd v. Adhill Properties Ltd* [1991] 61 P & CR 111, CA; Mance LJ in *MCI Worldcom International Inc. v. Primus Telecommunications plc* [2004] EWCA Civ 957; [2004] All ER (Comm) 833, at [30].

22 If the representor is not a party, he might be liable in deceit or negligence at common law: *Chitty on Contracts* (30th edn, London, 2008), 6-077.

23 *Chitty on Contracts* (30th edn, London, 2008), 6-028, 6-029.

24 (1861) 2 J & H 1, 22-3.

25 (1873) 6 HL 377.

26 [1896] 1 QB 372, CA.

27 *Smith v. Bush* [1990] 1 AC 831, 848, 856, 865, 871-2, HL.

28 J. Cartwright, *Misrepresentation, Mistake and Non-Disclosure* (2nd edn, London, 2007), 62.

29 [2000] 1 All ER (Comm) 573; [2000] Lloyd's Rep IR 535, at [17]; note Rix J's refusal to engage in 'microscopic' scrutiny of each phrase's accuracy at [200] and [201].

Arguably, this is merely an offshoot of the requirement of ‘materiality’ rather than a separate element.

(9) *If only the representee understood it in a sense that would be false, the statement will be a misrepresentation even though the parties placed different interpretations on it.* This is subject to the proviso that the representee’s approach (involving falsity) was objectively reasonable (but, in *EA Grimstead & Son Ltd v. McGarrigan* (1999),³⁰ the representee failed to show that he had construed information concerning the state of a business in a way which would constitute a misrepresentation, and he also failed to show that his suggested interpretation would have been objectively reasonable).

(10) *The statement is normally false when made and remains so at all stages prior to formation of the contract.* On the special situation where an initially accurate statement is falsified by supervening events, before the contract is formed, see 9.03.

(11) *The representee must be both (a) aware of the statement and (b) decisively influenced by it.* But there is an exception to proposition (b) if the statement was made fraudulently. The *basic propositions* concerning ‘reliance’ or inducement are:³¹

- (a) Reliance must be proved by the representee (except if the statement is fraudulent) but the law infers from a ‘material’ misrepresentation that there has been reliance; this requires the statement to have been a decisive reason for the representee entering the contract (except if the statement is fraudulent). It need not be the sole reason for his entering the contract. The fact that the representor might have checked the information is no bar to showing reliance.
- (b) If the statement is fraudulent, reliance is inferred; again if fraud is shown, the representation need not even have been a decisive factor.
- (c) In all cases (even if the statement is fraudulent), it is possible for the representor to counter the representee’s allegation of reliance by showing that in fact the representor was either unaware of the statement, or did not act on it, preferring instead to conduct his own inquiries, or he clearly affirmed that he had absorbed a correction (normally sent by the representor).

9.03 *Statement becoming false after initial affirmation but before formation of contract.* Sometimes an initially accurate statement is rendered inaccurate by a change of circumstances. Does the representor become liable in such circumstances? There are three views of this issue:

- (1) *Need for knowledge.* One view is that the representor becomes liable only if he discovers the change before the contract’s formation but fails to correct his earlier statement. This approach was adopted by Romer LJ and Clauson J in *With v. O’Flanagan* (1936).³² Indeed, it is arguable that this failure to correct will involve

30 [1988–99] Info TLR 384, CA (CA, 27 October 1999; transcript No. 1733 of 1999, pp. 19, 27).

31 For an expansion of these points, see 9.04.

32 [1936] Ch 575, 586, CA.

fraud.³³ Bigwood supports the criterion of 'knowledge'. He contends that the representor only makes a misrepresentation if he discovers the supervening falsification.³⁴ Chitty³⁵ favours Bigwood's approach.

- (2) *Criterion of fault.* Another view is that the representor becomes liable only if he ought reasonably to have discovered the change of circumstances. Treitel hints³⁶ at this intermediate view, that is, that the representor might owe a duty of care to take reasonable steps to check continuing accuracy of statement; this is based upon the notion of a 'reasonable' obligation to review the continuing accuracy or otherwise of one's pre-contractual statements. On this basis, it is arguable that the wording of section 2(1) of the Misrepresentation Act 1967 (9.14) imposes a duty on the representor to keep under review, at least to a reasonable extent, the veracity of his statements, although that duty ceases to apply once the contract has been formed. In the absence of 'reasonable grounds', the representor would become liable under that provision if a pre-contractual change of events, or perhaps perception, had falsified the earlier statement. Furthermore, Treitel contends that at common law a party might have assumed a duty to conduct such a review.
- (3) *Strict responsibility.* A third view is that pre-formation falsification of an initially accurate statement creates a 'misrepresentation' even if the representor is unaware of this change. The rationale of this approach is that the representation is deemed to be continuous until the contract is formed; and so it can be automatically falsified by a change of circumstances, whether or not the representor had any control over these events, and irrespective of his awareness of the relevant change. Lord Wright in *With v. O'Flanagan* (1936) approached the question either on the basis that liability hinges on the representor acquiring such knowledge of falsity (approach (1) above) or on the basis that he commits a representation irrespective of such knowledge (approach (3) now under discussion).³⁷ Cartwright supports this last approach. He contends that the uncorrected statement should be treated as a (non-fraudulent) misrepresentation at the date of the contract's formation, on the basis that it is impliedly repeated on each date subsequent to its making and before the contract's formation, and regardless of the representor's knowledge.³⁸ Cartwright argues attractively that this approach would be consistent with the law's treatment of a misrepresentation as an inaccurate statement whether or not it was accompanied by any culpability by the representor.

The choice between these three approaches awaits judicial clarification. As mentioned, Lord Wright in *With v. O'Flanagan* (1936) supported both approach (1) and approach (3),³⁹

33 In *Banks v. Cox* [2002] EWHC (Ch) 2166, at [4], where Lawrence Collins J held that this is a case of fraud; see also *Chitty on Contracts* (30th edn, London, 2008), 6-018 n. 89 on this point.

34 R. Bigwood, [2005] CLJ 94.

35 *Chitty on Contracts* (30th edn, London, 2008), 6-018.

36 *Treitel* (12th edn, London, 2007), 9-152.

37 [1936] Ch 575, 583, CA.

38 J. Cartwright, *Misrepresentation, Mistake and Non-Disclosure* (2nd edn, London, 2007), 4.27.

39 [1936] Ch 575, 583, CA.

whereas the majority, Romer LJ and Clauson J, did not discuss approach (3).⁴⁰ In one recent Court of Appeal case, *Spice Girls Ltd v. Aprilia World Service BV* (2002), Sir Andrew Morritt V-C assumed that approach (1), knowledge, was the test.⁴¹

When assessing which of these three approaches is to apply, it is submitted that the two different remedies of rescission and damages should be kept in mind:

- (a) As for the right to *rescind*, approach (3) should govern: such a right should arise without the need to show knowledge or fault. As for the second remedy, *damages*, approach (2) should govern.
- (b) As for the question of *damages*, in the absence of a contractual warranty concerning the continuing accuracy of a statement, liability to pay compensation should require *fault* (absence of 'reasonable grounds' for a continuing belief in the accuracy of the statement, under section 2(1) of the Misrepresentation Act 1967, 9.14), but this need not be *knowledge* (that being the criterion in approach (1)). Instead, fault can involve *failure to take reasonable steps to monitor the statement's continuing accuracy*. It should be enough that this failure was unreasonable in the relevant context; not every failure to discover will necessarily involve fault; it is likely that the courts will be inclined (as suggested by the wording of section 2(1)) to place the burden of proof on the representor; it will be incumbent on him to show that he was not guilty of fault in this respect.

9.04 Reliance and inducement in detail

For the basic propositions, see 9.02 above at point (11).

(1) *Need for 'reliance'*. The representee must rely on the misrepresentation: in simple terms, he must have been aware of the false statement and have been misled by it. The more common form of reliance is for the representee to be influenced to enter the contract.⁴² But another possibility is that, although the representee had already decided to enter the contract, he was misled by the misrepresentation into accepting a final set of terms less advantageous to him than he might otherwise have achieved.⁴³

No reliance occurs if the representee makes his own independent judgement concerning the relevant matter and so is not influenced by the representor's inaccurate words.

This last point was explained by the Court of Appeal in the *Peekay* case (2006) where a non-fraudulent misrepresentation, concerning the nature of a proposed investment, was made in a 'rough-and-ready' fashion.⁴⁴ The representee, a 'sophisticated' investor with

⁴⁰ *Ibid.*, at 586.

⁴¹ [2002] EWCA Civ 15; [2002] EMLR 27, at [51].

⁴² The fact that the representee's agent is aware can be decisive: *Strover v. Harrington* [1988] Ch 390, Browne-Wilkinson J.

⁴³ E.g. *Clef Aquitaine SARL v. Laporte Materials (Barrow) Ltd* [2001] QB 488, CA (9.13: misrepresentation had the effect of depressing the representee's overall level of profit); *Huyton SA v. Distribuidora Internacional de Productos Agrícolas SA* [2003] EWCA Civ 1104; [2003] 2 Lloyd's Rep 780, at [55] ff.

⁴⁴ *Peekay Intermark Ltd v. Australia and New Zealand Banking Group Ltd* [2006] EWCA Civ 386; [2006] 2 Lloyd's Rep 511 (controversially explained by *Treitel* (12th edn, London, 2007), 9-020, as a derogation from the principle in *Redgrave v. Hurd* (1881) 20 Ch D 1, CA; *Treitel's* comment is a misreading of Moore-Bick LJ's discussion in the *Peekay* case at [52]); the *Peekay* case was considered by Gloster J in *JP Morgan Chase Bank v. Springwell Navigation Corporation* [2008] EWHC 1186 (Comm), at [482].

extensive experience, had made up his mind to invest without reliance on this rather casual misrepresentation; instead, he believed that he knew the nature of the subject matter and that there was no need, therefore, for him to check the manner in which the investment had been described in the other party's document.⁴⁵

(2) *Relevance of 'materiality'*. The burden of proof is on the representee to show that he did rely on the misrepresentation. But, if he shows that the statement was 'material', in the sense that it would have normally influenced a person in the relevant situation to enter the contract, the representee is effectively 'home and dry' on this point (that is, unless the representor can show (1) that the representee did not allow the statement to enter at all into his decision-making, because the latter made investigations of his own; or (2) that the representee was in fact unaware of the representation). Thus, the function of 'materiality' is that it adds considerable momentum to the representee's cause: on this basis the law draws a common-sense inference that the representee, influenced by the statement, decided to enter this particular contract.

In *Spice Girls Ltd v. Aprilia World Service BV* (2002),⁴⁶ Sir Andrew Morritt V-C said:

It is sufficient that the misrepresentation is a material inducement, it does not have to be the only one. In *Smith v. Chadwick* (1884) 9 AC 187, 196 Lord Blackburn said: '[I]f it is proved that the defendants with a view to induce the plaintiff to enter into a contract made a statement to the plaintiff of such a nature as would be likely to induce a person to enter into a contract, it is a fair inference of fact that he was induced to do so by the statement.' Lord Blackburn went on to point out that the inference was one of fact not law and that if no evidence is given as to reliance in fact that was ground for not drawing the inference.

What does this mean? The position can be summarised as follows:

- (a) 'materiality' can be sufficient to establish reliance, provided the representee alleges that he did rely;
- (b) but it is not decisive, because other factors might be adduced by the representor to counter the inference of fact;
- (c) nor is 'materiality' necessary, because a representee might exceptionally be able to substantiate a plea of reliance without resort to this factor;
- (d) fraud enables the representee to demonstrate that he was induced to enter the contract (see further point (7) ('Position if statement is fraudulent') below).

As for (c), without the assistance of 'materiality', the representee's task in showing reliance on a non-fraudulent misrepresentation is an uphill struggle because he will need to adduce independent evidence that the statement had the effect of inducing him to enter into the relevant transaction. That will be difficult because, *ex hypothesi*, he is claiming to

45 *Peekay Intermark Ltd v. Australia and New Zealand Banking Group Ltd* [2006] EWCA Civ 386; [2006] 2 Lloyd's Rep 511, at [52], *per* Moore-Bick LJ.

46 [2002] EWCA Civ 15; [2002] EMLR 27, at [70].

have relied on something which would not have influenced others in the ordinary course of things.

(3) *Decisive influence*. Unless the statement involved fraud (see point (7) below; and, for the definition of deceit, see 9.12), the representee must have been decisively influenced by it: the so-called 'but for' test of causation applies⁴⁷ (although one commentator seems to disagree).⁴⁸ This means that the representation must have been operative on the representee's mind so that it made a crucial difference either *in determining that he would enter the contract*, or *that he would do so on a particular basis rather than on another basis*.

As Clarke LJ explained in *Assicurazioni Generali SpA v. Arab Insurance Group (BSC)* (2002) (the following passage assumes a material non-disclosure in the law of insurance, but the analysis applies equally where there is a positive misrepresentation by words or conduct):⁴⁹

I would summarise the relevant principles of inducement in this context in this way:

a) In order to be entitled to avoid a contract of insurance or reinsurance, an insurer or reinsurer must prove on the balance of probabilities that he was induced to enter into the contract by a material non-disclosure or by a material misrepresentation.

b) There is no presumption of law that an insurer or reinsurer is induced to enter in the contract by a material non-disclosure or misrepresentation.

c) The facts may, however, be such that it is to be inferred that the particular insurer or reinsurer was so induced even in the absence of evidence from him.

d) In order to prove inducement the insurer or reinsurer must show that the non-disclosure or misrepresentation was an effective cause of his entering into the contract on the terms on which he did. He must therefore show at least that, but for the relevant non-disclosure or misrepresentation, he would not have entered into the contract on those terms. On the other hand, he does not have to show that it was the sole effective cause of his doing so.

And Staughton LJ said in the same case:⁵⁰

I have had regard to the classic speech of Lord Mustill in *Pan Atlantic Insurance Co. Ltd v. Pine Top Insurance Co. Ltd* [1995] 1 AC 501, 549, and I hope that I have followed it. A misrepresentation or non-disclosure which did not make any difference, in the sense that the underwriter would have agreed to the same contract on the same

⁴⁷ *Chitty on Contracts* (30th edn, London, 2008), 6-034, for a review of the authorities.

⁴⁸ As for (1), *per contra* M. Chen-Wishart, *Contract Law* (2nd edn, Oxford, 2008), 212, citing *Re Leeds Bank* (1887) 56 LJ Ch 321.

⁴⁹ [2002] EWCA Civ 1642; [2003] 1 All ER (Comm) 140, at [62] (passage not included at [2003] 1 WLR 577).

⁵⁰ *Ibid.*, at [187].

terms if it had never been made, cannot be an inducement ... Causation cannot in law exist when even the 'but for' test is not satisfied.

(4) *The misrepresentation need not be the sole inducement.* The statement (unless fraudulent) must be decisively influential: either because it induced the representee to enter the contract, or at least to assent to the present set of terms (compare the facts of *Clef Aquitaine SARL v. Laporte Materials (Barrow) Ltd* (2001),⁵¹ discussed at 9.13 below, where the dispute concerned not the decision to contract, but the level of profit, with or without fraud). But the statement need not be the sole inducement: it is enough that it was one of the factors which induced the representee to enter the contract, or to assent to the present set of terms.⁵²

(5) *Representee can omit to check.* The rule in *Redgrave v. Hurd* (1881) is that the representation is actionable (giving rise to rescission, for example) even though the representee might have checked the information for himself⁵³ (although leading commentators advocate modification of this approach when the issue is whether the representor *should be liable to compensate for non-fraudulent statements*).⁵⁴

(6) *Correction.* The representor's attempted correction must hit home: it is not enough to attempt to correct a misrepresentation if the attempted correction does not in fact come to the representee's notice. In *Assicurazioni Generali SpA v. Arab Insurance Group* (2002), Clarke LJ said:

[I]t will in each case be a question of fact whether the misrepresentation was corrected so as to ensure that the corrected facts came to the knowledge of the [representee] or whether, when the contract was made, [the representee] was induced to make it by the original material misrepresentation or non-disclosure.⁵⁵

The representor can escape liability by requiring the other party to sign a declaration that he has indeed read a correction. In the *Peekay* case, the representee had signed a declaration that he had read and understood the document's accurate description of the subject matter. The Court of Appeal held that this precluded him from asserting that he had not read that correction.⁵⁶

(7) *Position if statement is fraudulent.* If the representee was the victim of *fraud* (provided the representee was aware of the statement and did not choose deliberately to

51 [2001] QB 488, CA.

52 *Edgington v. Fitzmaurice* (1885) 29 Ch D 459, CA; on which see *Standard Chartered Bank v. Pakistan Corporation (Nos. 2 and 4)* [2003] 1 AC 959, HL, at [14] to [19], *per* Lord Hoffmann; *Treitel* (12th edn, London, 2007), 9-022, notes Lord Hoffmann's suggestion, *ibid.*, at [17], that this is restricted to fraud.

53 *Redgrave v. Hurd* (1881) 20 Ch D 1, CA; *Standard Chartered Bank v. Pakistan Corporation (Nos. 2 and 4)* [2003] 1 AC 959, HL, at [14] to [19], *per* Lord Hoffmann.

54 *Chitty on Contracts* (30th edn, London, 2008), 6-039 to 6-040; *Treitel* (12th edn, London, 2007), 9-20 (representee culpably failing to check), considering statements in *Smith v. Eric S Bush* [1990] 1 AC 831, 854, 872, HL.

55 [2002] EWCA Civ 1642; [2003] 1 WLR 577; [2003] 1 All ER (Comm) 140, at [64] (passage cited in *Peekay* case, [2006] EWCA Civ 386; [2006] 2 Lloyd's Rep 511, at [36]).

56 *Peekay* case, [2006] EWCA Civ 386; [2006] 2 Lloyd's Rep 511, at [52], *per* Moore-Bick LJ, and at [66] ff, *per* Chadwick LJ; the third judge, Collins J, agreed.

ignore it), the statement is presumed to induce reliance, as the Court of Appeal noted in *County Natwest Bank Ltd v. Barton* (1999):⁵⁷

The rationale for the courts' willingness to lean in favour of the representee is that the other party has been especially heinous. As Lord Hobhouse observed in *Reeves v. Commissioner for Metropolitan Police* (2000): 'Where the defendant has set out to deceive the plaintiff, the success of that deception even though others might not have been deceived does not render the plaintiff's loss too remote; intended consequences are not too remote.'⁵⁸

3. STATEMENTS BECOMING EITHER TERMS OR 'COLLATERAL WARRANTIES'

- 9.05 To obtain 'loss of bargain' damages (18.45), the representee might contend that a pre-contractual misrepresentation has become (1) a 'contractual' term within the main contract or (2) a 'collateral warranty',⁵⁹ that is, a side contract subsisting independently of the main contract. The essence of (1) and (2) is that the maker of the statement or assurance is guaranteeing or contractually affirming its accuracy. Loss of bargain damages will place the representee in the position he would have enjoyed if the statement had been true. Furthermore, a warranted assurance is a cast-iron commitment. It imposes strict liability, regardless of proof of fraud or carelessness. And the defence of contributory negligence does not apply to breach of strict contractual obligations (18.50), such as breach of a warranty.
- 9.06 For example, suppose the defendant vendor said: 'This is a genuine "Louis XVI" sideboard.' If that statement had been accurate, the sideboard would have been worth £30,000. In fact, it was a later piece, worth only £1,000. The statement is likely to be a term of the contract under section 13(1) of the Sale of Goods Act 1979 (correspondence with description).⁶⁰ If so, the representee will be entitled to compensation for the difference between these sums. This will be the approach unless, quite exceptionally, the purchaser was clearly acting solely on his own superior knowledge.⁶¹

57 *The Times*, 29 July 1999, CA; *UCB Corporate Services v. Williams* [2002] EWCA Civ 555; [2003] 1 P & CR 12, at [86], citing *Downs v. Chappell* [1997] 1 WLR 426, 438, CA, *per* Hobhouse LJ; *Barton v. Armstrong* [1976] AC 104, 118–19, PC, drawing an analogy between duress as to person and fraud (on that case's significance in the law of duress, see 11.12); generally, *Chitty on Contracts* (30th edn, London, 2008), 6–034.

58 [2000] 1 AC 360, 394 A, HL, *per* Lord Hobhouse.

59 K. W. Wedderburn, 'Collateral Contracts' [1959] CLJ 58; *Chitty on Contracts* (30th edn, London, 2008), 12–103; Paterson, *Collateral Warranties Explained* (London, 1991); D. W. Greig, (1971) 87 LQR 179.

60 *Beale v. Taylor* [1967] 1 WLR 1193, CA (private seller's description of car as '1961, Herald 1200 convertible'; in fact car made of two halves welded together; only the back half was a '1200' model; statement treated as term of the main contract).

61 *Harlingdon & Leinster Enterprises v. Christopher Hull Fine Art* [1991] 1 QB 564, CA (purchaser was an expert and placed no reliance on the seller's attribution of a painting).

9.07 *Criteria for finding 'contractual assurances'*. The test governing the finding of a collateral warranty remains strict (despite Lord Denning's suggestion in *Howard Marine v. Ogden* (1978) that a more flexible approach be adopted).⁶² Thus, consistent with this strict approach, the Court of Appeal in *Business Environment Bow Lane Ltd v. Deanwater Estates Ltd* (2007)⁶³ (9.08) cited Lord Moulton's seminal comment in the *Heilbut, Symons* case (1913):⁶⁴

Such collateral contracts, the sole effect of which is to vary or add to the terms of the principal contract, are therefore viewed with suspicion by the law. They must be proved strictly. Not only the terms of such contracts but the existence of an *animus contrahendi* [an intention to make a contractual undertaking] on the part of all the parties to them must be clearly shown. Any laxity on these points would enable parties to escape from the full performance of the obligations of contracts unquestionably entered into by them and more especially would have the effect of lessening the authority of written contracts by making it possible to vary them by suggesting the existence of verbal collateral agreements relating to the same subject matter.

In particular, the courts will consider the following criteria:⁶⁵

- (1) *Objective commitment by maker of statement*. The court will conduct an objective assessment of whether the representee was entitled reasonably to assume that the statement was being warranted, that is, guaranteed to be contractually binding.⁶⁶
- (2) *Importance to representee emphasised*. The court will consider whether the representee made plain that the matter was crucial to him.⁶⁷
- (3) *Obvious importance*. Whether it was obvious from the circumstances that the matter was crucial to the representee. Thus, in *City & Westminster Properties (1934) Ltd v. Mudd* (1959), the landlord assured a tenant, before a renewal to him of a tenancy, that he would be free to sleep in the demised business premises at night; this was contrary to the written terms of the lease; Harman J was convinced by the tenant's

62 *Howard Marine and Dredging Co. Ltd v. A Ogden & Sons (Excavations) Ltd* [1978] QB 574, 590G, CA.

63 [2007] EWCA Civ 622; [2007] L & TR 26, at [23].

64 *Heilbut, Symons & Co. v. Buckleton* [1913] AC 30, 47, HL (see also Lord Haldane at 37–9); citing *Chandelor v. Lopes* (1603) Cro Jac 4; explained by Denning LJ in the *Oscar Chess* case, [1957] 1 WLR 370, CA; see also *Hopkins v. Tanqueray* (1854) 15 CB (NS) 130.

65 Cf the string of factors successfully enumerated by counsel in the *Howard Marine* case, [1978] QB 574, 583, CA: whether the statement is clear and definite; whether intended to be a guarantee; whether evidence of contractual intention; whether incorporated expressly into the final contract; whether a matter of opinion or an estimate; whether contemporaneous with contract or weeks or months prior thereto; whether within the representor's knowledge and conversely whether the representee could reasonably be expected, or able, to ascertain it; whether inconsistent with the written terms of the final contract.

66 *Thake v. Maurice* [1986] QB 644, CA (3.71); reasonableness is also a factor in the tort of negligent misstatement: *Williams v. Natural Life & Health Foods* [1998] 1 WLR 830, 837, HL.

67 E.g. *Bannerman v. White* (1861) 10 CB (NS) 844 (prospective buyer asking whether sulphur had been used in cultivation of hops; seller saying 'no'; it was clear that the purchaser would have walked away if the hops had been sulphurated; therefore the assurance had contractual effect).

evidence that the matter covered by this oral assurance had been a potential 'deal-breaker'. He held that the oral assurance should take effect as a collateral warranty; the effect of this warranty was that it was not possible for the landlord to forfeit the lease for breach of the covenant (contained in the formal written terms of the tenancy) not to reside there at night.⁶⁸

- (4) *The court will consider the relative skill, knowledge and expertise of the parties.*⁶⁹ In *Dick Bentley Productions v. Harold Smith (Motors)* (1965),⁷⁰ the Court of Appeal held that a car dealer's statement that a car had covered 20,000 miles since a new engine had been fitted was a contractual warranty. In fact, the car's true mileage since that engine had been fitted was 100,000 (see also *Esso Petroleum Ltd v. Mardon* (1976)).⁷¹ By contrast, in *Oscar Chess Ltd v. Williams* (1957),⁷² no warranty was established when a private vendor, basing himself on a logbook which had been forged by a third party, said in good faith that a car was a 1948 model, when in fact it was a 1939 model; the buyer was an experienced car dealer.
- (5) *Independent verification urged.* The court will consider whether the representor asked the representee to verify the matter for himself.⁷³
- (6) *Need for independent verification expressly negatived.* Conversely, the court will take into account whether the representor assured the other that such verification was unnecessary.⁷⁴
- (7) *A representation of fact is much more likely intended to have contractual effect than a statement of future fact or future forecast.*⁷⁵ In fact, this is no more than a vague rule of thumb. Certainly, predictions can sometimes involve collateral warranties. For example, in *Esso Petroleum Co. Ltd v. Mardon* (1976),⁷⁶ a forecast was held to involve a collateral warranty that the maker of it had reasonable grounds for believing the accuracy of his prediction. Esso had made a statement concerning a filling station's likely level of customer demand (a 'throughput' of 200,000 gallons). This forecast was treated as a collateral warranty that Esso had reasonable grounds for making the prediction. But the statement was not regarded as a guarantee of that predicted level. (A second and alternative basis of decision was that Esso had breached a tortious duty of care and that it was therefore liable to compensate for their negligent misstatement.)

68 [1959] Ch 129, 145–6, Harman J.

69 *Harlingdon & Leinster Enterprises v. Christopher Hull Fine Art* [1991] 1 QB 564, CA (where the purchaser was an expert and placed no reliance on the seller's attribution of a work of art to a particular painter).

70 [1965] 1 WLR 623, CA.

71 [1976] QB 801, CA.

72 [1957] 1 WLR 370, CA (Morris LJ dissenting).

73 *Ecay v. Godfrey* [1947] Lloyd's Rep 286, Lord Goddard CJ (seller of second-hand boat making clear his belief that the purchaser would be having it surveyed first); cf where the defendant encouraged the plaintiff to rely on his assurance without further inquiry or verification (see next note) in *Schawel v. Reade* [1913] 2 IR 64, HL.

74 *Schawel v. Reade* [1913] 2 IR 64, HL ('you need not look for anything; the horse is perfectly sound. If there were anything the matter with the horse, I should tell you.').

75 *Business Environment Bow Lane Ltd v. Deanwater Estates Ltd* [2007] EWCA Civ 622; [2007] L & TR 26, at [23].

76 [1976] QB 801, CA.

- (8) *Timing*. The lapse of time between the statement and the making of the formal contract will be a factor to be taken into account. In general, 'the longer the interval, the greater the presumption must be that the parties did not intend the statement to have contractual effect in relation to a subsequent deal'.⁷⁷
- (9) *Subsequent negotiation superseding informal statement*.⁷⁸ The court will look at whether the statement is followed by further negotiations and a written contract not containing any term corresponding to the statement. In such a case, it will be harder to infer that the statement was intended to have a contractual effect because the *prima facie* assumption will be that the written contract includes all the terms the parties wanted to be binding between them.

9.08 No collateral warranty arose in the *Business Environment* case (2007).⁷⁹ The Court of Appeal held that the final version of a lease contained a clause which had superseded a surprisingly generous earlier written concession, relieving the tenant of liability for dilapidations. And so the concession did not take effect.

During negotiations for a commercial lease, the tenant received a written assurance from the landlord that the tenant would not be liable for dilapidations (payment for repairs attributable to the tenant's use of the premises) at the end of the lease. Releasing the tenant from this liability would be a surprisingly generous concession by the landlord.

The Court of Appeal held that this written assurance had been superseded by a clause inserted into the final lease. This clause restored the landlord's right to require payment for dilapidations. Sir Andrew Morritt V-C said⁸⁰ 'the representation relied on related to future events in unforeseeable circumstances', and such a 'commitment ... would be wholly uncommercial'. The other two judges, May and Lloyd LJ, said that the informal assurance had been superseded by further negotiations culminating in a settled and agreed form of wording in the final lease.

9.09 *Collateral warranties and the 'parol evidence rule'*. Such 'side-agreements', subsisting independently of the main contract, form an exception to the parol evidence rule (14.26 ff).⁸¹ This long-standing evidential rule operates to bar parties from adducing 'extrinsic evidence', whether oral or written, for the purpose of supplementing, varying or contradicting

77 *Business Environment Bow Lane Ltd v. Deanwater Estates Ltd* [2007] EWCA Civ 622; [2007] L & TR 26, at [23] (adopting Lightman J's statement in *Inntrepeneur Pub Co. Ltd v. East Crown Ltd* [2000] 2 Lloyd's Rep 611, 615); the *Business Environment* case also notes: *Henderson v. Arthur* [1907] 1 KB 10, CA, *City & Westminster Properties (1934) Ltd v. Mudd* [1959] 1 Ch 129 (Harman J) and *Brikom Investments v. Carr* [1979] 1 QB 467, CA.

78 *Business Environment Bow Lane Ltd v. Deanwater Estates Ltd* [2007] EWCA Civ 622; [2007] L & TR 26, at [23].

79 [2007] EWCA Civ 622; [2007] L & TR 26, at [23].

80 *Ibid.*, at [47].

81 *Treitel* (12th edn, London, 2007), 6-012 ff; Law Commission, *The Law of Contract: The Parol Evidence Rule* (Law Commission Report No. 154, Cmnd 9700, London, 1986), 2.32 to 2.36 (noted by G. Marston, [1986] CLJ 192).

the contract's written terms. The rule safeguards the primacy of the agreed text. And so its purpose is to promote certainty, accessibility and finality.

However, a collateral warranty is not a violation of the parol evidence rule because the extrinsic evidence is admitted for the purpose of establishing an independent agreement rather than a variation of the main agreement. It will be seen immediately that use of collateral warranties to evade the parol evidence rule is a 'dodge', a device designed to inject equity or informality into the context of written contracts.

In fact, businessmen, in the interests of certainty and completeness, often insert into commercial written contracts an 'entire agreement' clause (9.27). Such a clause declares that the final contract contains all relevant contractual terms and assurances or understandings. The result is that collateral agreements are denied any force.

- 9.10 *Collateral warranties and the (common law) privity problem.* Collateral warranties can be used to circumvent problems arising from absence of 'privity of contract' (see 7.03 for the common law rule that a third party cannot sue on a contract).

In *Shanklin Pier Ltd v. Detel Products Ltd* (1951), a supplier of paint (A) was held to have warranted to a pier-owner (B) the fitness of A's paint for painting piers. B relied on this when he stipulated that X, the contractor commissioned to paint the pier, should use A's paint. The upshot was that A was liable to B to compensate for the poor quality of the paint used, even though X bought the paint directly from A.⁸²

Other cases provide further illustrations:

In *Andrews v. Hopkinson* (1957),⁸³ a car dealer said: 'It's a good little bus; I'd stake my life on it.' The main contract was between a finance company and the purchaser. McNair J found a collateral warranty between the dealer and the purchaser.

In *Wells (Mertsham) v. Buckland Sand & Silica Ltd* (1965),⁸⁴ a sand supplier warranted the fitness of sand for particular horticultural use ('the assurance'). In fact, not all deliveries of the sand were made under a contract of sale with that supplier. But Edmund-Davies J found a collateral warranty that the sand should comply with the assurance.

In *Charnock v. Liverpool Corporation* (1968),⁸⁵ the plaintiff's car was repaired under a contract between the garage and the plaintiff's insurance company. The plaintiff (not a party to the contract) was reassured by the garage that the car would be ready quite soon. The Court of Appeal held that there was a collateral warranty that the car would be repaired within a reasonable period.

82 [1951] 2 KB 854, McNair J.

83 [1957] 1 QB 229, McNair J.

84 [1965] 2 QB 170, Edmund-Davies J.

85 [1968] 1 WLR 1498, CA.

4. DIFFERENCES BETWEEN COMPENSATION UNDER THE MISREPRESENTATION ACT 1967 (OR IN TORT) AND FOR BREACH OF CONTRACT

- 9.11 There is a difference between the aim or function of ‘tort’ damages (namely, compensation awarded, in the present context, for the torts of deceit or negligence or under section 2(1) of the Misrepresentation Act 1967, cited at 9.14), and contractual damages for breach of warranties or similar contractual assurances or undertakings.⁸⁶ Contractual damages give the claimant the difference between the actual value of the subject matter on completion and its warranted value. This is the basic ‘loss of bargain’ measure (18.25). For example, if a vendor, V, sells a business to a purchaser, P, and warrants that the volume of business has been and/or will continue to be at level £x, P can sue only in contract, not in tort, for the difference between the revenue which would have been generated if the warranty had been accurate and the lower level in fact achieved. That type of ‘pure expectation’ is created only by a contractual term or a collateral warranty, and the expectation is protected by contractual damages for breach of such an undertaking. Even if the warranty were made fraudulently, the representee’s damages *in tort* would not be based on the difference between the subject matter delivered and the subject matter’s higher value *as warranted*: only contractual damages protect the warranted value.

Tort damages⁸⁷ (see further 9.12) are aimed at placing the representee in the position in which he would have been if the culpable misrepresentation had not been made. This provides the injured party with the difference in value between the price paid and the subject matter’s lesser and actual value at the date of completion. This ‘capital’ loss can be supplemented by an award of ‘consequential’ loss, such as money lost in running the defective business or money not gained from pursuing an alternative business (these are ‘income losses’; but consequential harm could embrace other forms of loss which flow from a fraudulent or negligent misrepresentation, such as damage to property or even personal injury). Tort claims are attractive if the transaction was a bad bargain, that is, the purchaser had agreed to pay too much because the price would have exceeded the subject matter’s actual value even if it had corresponded to its warranted quality.

5. COMPENSATION IN THE TORT OF DECEIT

- 9.12 The tort of deceit requires a representation to be made without an honest belief in its accuracy. Failure to take care to verify is not enough to constitute deceit, provided the representor has the honest belief that what he asserts is true. In *Derry v. Peek* (1889),

⁸⁶ *Smith New Court Securities Ltd v. Scrimgeour Vickers (Asset Management) Ltd* [1997] AC 254, 281–2, HL, per Lord Steyn.

⁸⁷ A claim for deceit, or under section 2(1) of the Misrepresentation Act 1967, or a common law claim for tortious negligence: generally, see A. Tettenborn (with D. Wilby and D. Bennett), *The Law of Damages* (London, 2003), chapter 17.

the House of Lords made clear that the *absence of an honest belief* is the essence of a fraudulent misrepresentation. In that case, in a passage which remains authoritative, Lord Herschell summarised the law as follows:⁸⁸

I think the authorities establish the following propositions: First, in order to sustain an action of deceit, there must be proof of fraud, and nothing short of that will suffice. Secondly, fraud is proved when it is shewn that a false representation has been made (1) knowingly, or (2) without belief in its truth, or (3) recklessly, careless whether it be true or false. Although I have treated the second and third as distinct cases, I think the third is but an instance of the second, for one who makes a statement under such circumstances can have no real belief in the truth of what he states.

To prevent a false statement being fraudulent, there must, I think, always be an honest belief in its truth. And this probably covers the whole ground, for one who knowingly alleges that which is false, has obviously no such honest belief. Thirdly, if fraud be proved, the motive of the person guilty of it is immaterial. It matters not that there was no intention to cheat or injure the person to whom the statement was made ...

In my opinion making a false statement through want of care falls far short of, and is a very different thing from, fraud, and the same may be said of a false representation honestly believed though on insufficient grounds.

A fraudulent statement is presumed to induce reliance (point (7) at 9.04).

As for the measure of damages for deceit, Lord Browne-Wilkinson in the leading decision, the *Smith New Court* case (1997), stated the general principles as follows:⁸⁹

[T]he defendant is bound to make reparation for all the damage directly flowing from the transaction; although such damage need not have been foreseeable, it must have been directly caused by the transaction ... as a general rule, the benefits received by him include the market value of the property acquired as at the date of acquisition, but [this date of acquisition] rule is not to be inflexibly applied where to do so would prevent him obtaining full compensation for the wrong suffered⁹⁰ ... the [date of acquisition rule] ... will normally not apply when either (a) the misrepresentation has continued to operate after the date of the acquisition of the asset so as to induce the plaintiff to retain the asset; or (b) the circumstances of the case are such that the plaintiff is, by reason of the fraud, locked into the property [point (b) here is a reference to the problem, as illustrated by the facts of the *Smith New Court* case, where it is not economic or even practicable for the representee immediately to rid himself of

⁸⁸ *Derry v. Peek* (1889) 14 App Cas 337, 374, HL.

⁸⁹ *Smith New Court Securities Ltd v. Scrimgeour Vickers (Asset Management) Ltd* [1997] AC 254, 266–7, HL, per Lord Browne-Wilkinson (Lord Mustill, *ibid.*, at 269G, said that Lord Browne-Wilkinson's propositions should supersede the statements in *Doyle v. Olby* [1969] 2 QB 158, CA, which Lord Mustill regarded as not wholly reliable authority); for a neat illustration of these principles, see *Banks v. Cox* [2002] EWHC (Ch) 2166, at [13] ff, per Lawrence Collins J.

⁹⁰ Noting, in contract law, *Johnson v. Agnew* [1980] AC 367, 401A, HL, and, in tort law, *Dodd Properties (Kent) Ltd v. Canterbury City Council* [1980] 1 WLR 433, CA.

the subject matter on discovering the deceit]. In addition, the plaintiff is entitled to recover consequential losses caused by the transaction.⁹¹

- 9.13 Deceit claims and 'income losses'.** A claimant can recover damages in the tort of deceit to compensate for uncovenanted 'income loss' or for 'lost opportunity for gain'.

In *East v. Maurer* (1991), the claimant bought a hairdressing salon after the defendant had deceitfully tricked her into believing that he would not continue working in his second, nearby, competing salon. In fact, he intended to continue working at his second salon.⁹² The damages awarded for deceit in this case included compensation for loss of the notional gain which the claimant would have made if she had instead invested her capital elsewhere in a similar but unproblematic salon, that is, a business not blighted by the defendant's decision to continue running a rival salon in the vicinity.

Commenting favourably on this case in the *Smith New Court* case (1997), Lord Steyn said that *East v. Maurer* 'shows that an award based on the hypothetical profitable business in which the plaintiff would have engaged but for deceit is permissible: it is classic consequential loss.'⁹³

In *Clef Aquitaine SARL v. Laporte Materials (Barrow) Ltd* (2001), the claimant took a distributorship to supply the defendant's products in France.⁹⁴ But the defendant had fraudulently misled the claimant as to the prices charged for these products in the UK. The Court of Appeal awarded the claimant the extra profit which it would have gained if the defendant had not fraudulently distorted the negotiations concerning the alleged lowest supply prices; in other words, compensation for a better deal that might have resulted from honest dealings with the same defendant.

In *4 Eng Ltd v. Harper* (2008),⁹⁵ the claimant was trying to decide which of two businesses to buy, either E or T. She decided to purchase E, a decision influenced by the defendant's fraudulent misrepresentations concerning E's trading performance. The claimant successfully claimed for the loss of the chance (18.32), reckoned by the judge at 80 per cent, to purchase T. The case is significant because it establishes that the *East v. Maurer* measure of loss for deceit extends to (1) loss of a chance to acquire an alternative particular business (as distinct from the certainty that an alternative, of a generic type, would have been acquired, as on the facts of the *East v. Maurer* case: see above); and (2) the claim in the *4 Eng Ltd* case extended beyond the income that would have been derived from running the alternative business to include the capital gain that would have accrued if, in due course, the alternative business had been sold by the claimant.

91 E.g. the facts of *Doyle v. Olby (Ironmongers) Ltd* [1969] 2 QB 158, CA.

92 [1991] 1 WLR 461, CA; noted J. Marks, (1992) 108 LQR 386.

93 *Smith New Court Securities Ltd v. Scrimgeour Vickers (Asset Management) Ltd* [1997] AC 254, 282, HL.

94 [2001] QB 488, CA.

95 [2008] EWHC 915 (Ch); [2009] Ch 91, David Richards J (noted by P. Mitchell, (2009) 125 LQR 12–17).

The Court of Appeal in *Parabola Investments Ltd v. Browallia Cal Ltd* (2010)⁹⁶ held that damages in the tort of deceit can extend to opportunities for investment which continue to be lost even after the relevant fraud has been discovered. The defendant admitted that one of its traders, B, had fraudulently misrepresented to the claimant (himself an established stock market trader) on a daily basis that the trading being conducted for the claimant's benefit was profitable, and also made a series of fraudulent misrepresentations as to the amount of the funds in the account administered by the defendant. That account declined over the period from £4.25m to £0.5m ('capital loss'). The defendant accepted vicarious liability for B's fraud. The claimant sought compensation not only (1) for the aforementioned capital loss but (2) for the loss of profits which the claimant would have made on alternative trading both during the period of the fraud and (3) during the period from discovery of the fraud until trial.

Item (1) was not in doubt. As for (2) and (3), the Court of Appeal upheld these claims. It held that the principle of compensation should be applied to achieve complete indemnification of the claimant's loss. The court supported this principle by reference to the *Smith New Court* case (1997), *East v. Maurer* (1991) and the *Sempra* case (2007).⁹⁷ That principle would apply subject to the subsidiary principles of causation (18.39), remoteness (18.40), mitigation (18.49) and the restriction against making damages awards for wholly 'speculative loss' (18.33).

6. DAMAGES UNDER SECTION 2(1) OF THE MISREPRESENTATION ACT 1967⁹⁸

9.14 *Damages are tortious and patterned on deceit without requiring proof of fraud.* Section 2(1) of the Misrepresentation Act 1967 reads:

Where a person has entered into a contract after a misrepresentation has been made to him by another party thereto and as a result thereof he has suffered loss, then, if the person making the misrepresentation would be liable in respect thereof had the misrepresentation been made fraudulently, that person shall be so liable notwithstanding that the misrepresentation was not made fraudulently, unless he proves that he had reasonable ground to believe and did believe up to the time the contract was made that the facts represented were true.

96 [2010] EWCA Civ 486; [2010] 3 WLR 1266 at [32] to [60], *per* Toulson LJ, with the agreement of Rimer and Mummery LJ; *Banks v. Cox* [2002] EWHC (Ch) 2166, at [13] ff, *per* Lawrence Collins J, also illustrates a 'loss of income' claim following a fraudulent misrepresentation (in the case itself, a fraudulent failure to correct a falsified statement).

97 *Parabola Investments Ltd v. Browallia Cal Ltd* [2010] EWCA Civ 486 at [32] to [60], *per* Toulson LJ, considering *Smith New Court Securities Ltd v. Scrimgeour Vickers (Asset Management) Ltd* [1997] AC 254, HL, *East v. Maurer* [1991] 1 WLR 461, CA, *Sempra Metals Ltd v. Inland Revenue Commissioners* [2007] UKHL 34; [2008] 1 AC 561 (on this case, see 18.64), and also considering *Hungerfords v. Walker* (1989) 171 CLR 125 (High Court of Australia).

98 P. S. Atiyah and G. H. Treitel, (1967) 30 MLR 369; P. Fairst, [1967] CLJ 239; see also R. Taylor, 'Expectation, Reliance and Misrepresentation' (1982) 85 MLR 138; I. Brown and A. Chandler, [1992] LMCLQ 40; R. Hooley, (1991) 107 LQR 547; A. Tettenborn (with D. Wilby and D. Bennett), *The Law of Damages* (London, 2003), chapter 17.

Damages under this provision are classified as tortious. This means that the representee cannot sue for his expectation interest (9.11, 18.25), that is, on the basis that the statement was a guarantee of accuracy. Sir Donald Nicholls V-C in *Gran Gelato Ltd v. Richliff Ltd* (1992) made two helpful observations on the nature of liability under this provision:⁹⁹ first, 'in short, liability ... is essentially founded on negligence, in the sense that the defendant, the representor, did not have reasonable grounds to believe that the facts represented were true'. Secondly, he said: 'Stated broadly, the measure of damages payable under [section 2(1)] is that sum of money which will place the plaintiff in the position he would have been in if the representation had not been made.'

Furthermore, the courts give effect to the so-called 'fiction of fraud' contained in section 2(1) of the 1967 Act (namely, the parenthetical phrase within section 2(1) which reads: 'if the person making the misrepresentation would be liable in respect thereof had the misrepresentation been made fraudulently ...'). The Court of Appeal in *Royscot v. Rogerson* (1991)¹⁰⁰ held that this curious 'fiction' dispenses with the general remoteness test applicable to negligence claims in tort (the 'reasonable foreseeability' formulation of a remoteness test).¹⁰¹ And so the representee can recover his loss, however unforeseeable, provided this loss is causally related to the misrepresentation; in other words, provided 'the chain of causation' has not been broken. The controversial, anomalous and indeed bizarre, availability of the fraud measure of damages for a merely careless misstatement led Rix J in *Avon Insurance plc v. Swire Fraser Ltd* (2000) to describe section 2(1) as a 'mighty weapon'.¹⁰²

However, this 'Royscot interpretation' might be reversed if section 2(1) were to come before the Supreme Court. The door seems ajar, for Lords Browne-Wilkinson and Steyn in *Smith New Court Securities Ltd v. Scrimgeour Vickers (Asset Management) Ltd* (1997)¹⁰³ expressed doubt concerning the *Royscot* case on this point.

These doubts rest on the fact that the *Royscot* case gives the representee a degree of protection which fails to reflect reality: the representor has been guilty of negligence or simple fault and not dishonesty. Lord Steyn in the *Smith New Court* case¹⁰⁴ approved Richard Hooley's comment¹⁰⁵ on the *Royscot* case as 'trenchant academic criticism'; Hooley describes the fraud measure under section 2(1) as 'repugnant' and 'bizarre'.

The source of this odd formulation (the 'fiction of fraud') seems to be this. The Law Reform Committee's report (July 1962)¹⁰⁶ was composed ten months before the tort of negligent misstatement was discovered in the *Hedley Byrne* case on 28 May 1963.¹⁰⁷ The 1962 Committee wished the draftsman to make clear that damages for misrepresentation

99 [1992] Ch 560, 573, 575.

100 [1991] 2 QB 297, CA.

101 'The Wagon Mound' [1961] AC 388, PC (summarised by Lord Rodger in *Simmons v. British Steel plc* [2004] UKHL 20; [2004] ICR 585, at [67]).

102 [2000] 1 All ER (Comm) 573; [2000] Lloyd's Rep IR 535, at [14], [200] and [201].

103 [1997] AC 254, 267F, 283, HL.

104 *Ibid.*, at 283, HL.

105 (1991) 107 LQR 547.

106 Law Reform Committee, *Innocent Misrepresentation* (Law Reform Committee 10th Report, Cmnd 1782, 1962).

107 [1964] AC 465, HL.

would not be based on a contractual warranty but on a tortious wrong. In this sense, the Committee suggested¹⁰⁸ that statutory compensation should be ‘no less extensive’ than deceit damages. At the time, deceit was the only species of tort damages available. Once the tort of negligent misstatement had arisen, and been declared applicable to the pre-contractual context (in *Esso Petroleum Ltd v. Mardon* (1976)),¹⁰⁹ the Delphic fiction of fraud had become an unfortunate anachronism.

For the moment, section 2(1) provides a representee-friendly route to compensation which is generously patterned on the tort of deceit (although not requiring proof of deceit: on that tort’s requirement, see 9.12).

Furthermore, once the claimant has shown that a statement was false, the defendant bears the burden of proof under section 2(1) of showing that he had reasonable grounds for believing the accuracy of his statement. According to one of the judges in the majority in *Howard Marine v. Ogden* (1978),¹¹⁰ the ‘burden of proof’ point was the only reason that the representor should be held liable on the facts of that case.

The damages claim in *Howard Marine v. Ogden* (1978) concerned an inaccurate statement of the capacity of two giant barges. The statement had been made after the representor had checked the relevant figures against Lloyd’s Register. But Lloyd’s had got it wrong. Furthermore, at trial, the representor’s manager admitted that, before making the fateful inaccurate statement, he had recollected a quite different figure in the vessel’s official specifications, contained in a document kept by his company. But, bizarrely, he had failed to appreciate that this other figure must have been accurate, and that the Lloyd’s Register figure was wrong. Bridge and Shaw LJ held that the representor had not done sufficiently diligent homework. He should have worried more about the discrepancy between these figures and worked out that the figure contained in his company’s specification document was the true one. And so liability under section 2(1) arose. Bridge LJ thought that, if it had been necessary to prove that the representor had been negligent at common law, the claim would have failed (although he offers no reasoning on this point), but, because the Act placed the burden on the representor to show ‘reasonable grounds’ for his belief, the statutory claim should succeed. Shaw LJ thought that the lack of competence shown on these facts would have rendered the representor liable at common law for negligence, but of course the statutory claim also succeeded. Lord Denning MR dissented, preferring Bristow J’s benevolent, or perhaps confused, decision at first instance that the representor had been right to be impressed by the Lloyd’s figure.

- 9.15 Another advantage for claimants under this provision is that they do not need to show a ‘special relationship’ or satisfy the common law requirement of an ‘assumption of responsibility’ (these are requirements for establishing a duty of care in the tort of

108 Law Reform Committee, *Innocent Misrepresentation* (Law Reform Committee 10th Report, Cmnd 1782, 1962), at [22].

109 [1976] QB 801, CA.

110 *Howard Marine and Dredging Co. Ltd v. A Ogden & Sons (Excavations) Ltd* [1978] QB 574, 590G, CA.

negligence: see 5.17 for a summary). In essence, the common law entitles a representee to recover damages for economic loss resulting from a negligent misstatement. The Court of Appeal in *Esso Petroleum Ltd v. Mardon* (1976)¹¹¹ recognised this possibility, acknowledging that tortious liability for negligent misstatements under the principle of *Hedley Byrne & Co. v. Heller* (1964)¹¹² extends to pre-contractual negotiations. But Sir Donald Nicholls V-C in *Gran Gelato Ltd v. Richliff Ltd* (1992)¹¹³ held that, although in some contexts an agent acting within his authority *might* assume a common law duty of care independently of his principal, this is *not so where*, as, on the facts of that case, a vendor's solicitor made a careless statement concerning the relevant property in a conveyancing transaction:

in normal conveyancing transactions solicitors who are acting for a seller do not in general owe to the would-be buyer a duty of care when answering inquiries before contract or the like ... The buyer is formally seeking information from the seller about the land and his title to it. The answers given by the solicitor are given on behalf of the seller. The buyer relies upon those answers as answers given on behalf of the seller ... I venture to think that in these circumstances one would expect to find [and, of course, this is axiomatic] that the law provides the buyer with a remedy against the seller if the answers were given without due care. I am far from persuaded that the fair and reasonable reaction to these facts is that there ought also to be a remedy against the other party's solicitor personally.

9.16 *Principal liable but not agent.* However, the only person liable under section 2(1) of the 1967 Act is the principal to a transaction, that is, the 'party' to the agreement: section 2(1) does not impose liability on the representor's *agent*.¹¹⁴ In other words, the person whose culpable 'belief' counts is the principal (the party to the contract and hence defendant) and not his agent (who in fact made the representation).¹¹⁵

9.17 *Defences to section 2(1) claims.* There are three defences to a claim under this provision.

- (1) The defendant might succeed in showing that he did have reasonable grounds for believing the accuracy of his statement, and that these grounds endured until the contract's formation.
- (2) The claimant might have failed to mitigate his loss (generally on the doctrine of mitigation, see 18.49). Here, the representee cannot recover loss to the extent that he might reasonably have mitigated that loss. The mitigation rule applies to a claim under section 2(1), as well as to a common law claim for deceit.¹¹⁶

¹¹¹ [1976] QB 801, CA.

¹¹² [1964] AC 465, HL.

¹¹³ [1992] Ch 560, 570.

¹¹⁴ *Resolute Maritime Inc. v. Nippon Kaiji Kyokai ('The Skopas')* [1983] 1 WLR 857, Mustill J.

¹¹⁵ *MCI WorldCom International Inc. v. Primus Telecommunications Inc.* [2004] 1 BCLC 42, Colman J, Commercial Court.

¹¹⁶ On the mitigation requirement in deceit, see *Smith New Court* case, [1997] AC 254, 267, HL, at proposition (7), *per* Lord Browne-Wilkinson; and *Downs v. Chappell* [1997] 1 WLR 426, CA.

- (3) The defendant's liability under section 2(1) can be reduced to take account of the claimant's contributory negligence, because the Law Reform (Contributory Negligence) Act 1945 (18.50) applies to such a claim.¹¹⁷ However, a representee's failure to check the accuracy of a representation is not an example of such contributory negligence:¹¹⁸

[I]t would need to be a very special case before carelessness by ... the representee would make it just and equitable to reduce the damages payable to compensate [that party] for loss suffered by it in consequence of doing the very thing which, in making the representation, [the defendant] intended should happen, viz., that [the claimant] should rely on the representation. In principle, carelessness in not making other inquiries provides no answer to a claim when the claimant has done that which the representor intended he should do. This is a well-established principle when misrepresentation, whether innocent or fraudulent, is being relied on as a ground for seeking rescission of the ensuing contract.

The 1945 Act, however, does *not* apply to the tort action for deceit.¹¹⁹

7. RESCISSION AB INITIO¹²⁰

- 9.18 Misrepresentation normally has the effect of rendering the contract open to rescission rather than a complete nullity. This reflects the distinction between a (supposed) void contract and a valid contract which exists until rescinded or set aside, that is, a voidable agreement.¹²¹ In the case of a void contract, there is no agreement to set aside. By contrast, the process of rescission (*ab initio*) of a voidable contract (also known as *restitutio in integrum*) involves restoring the parties to their pre-contractual position, that is, a reciprocal giving back and restoration, including, where applicable, indemnification as a substitute for, or to supplement, physical restitution (for financial adjustment to achieve complete restoration of benefits obtained, see 9.19).

Usually, rescission is normally effected without recourse to court proceedings. Such self-help rescission involves the 'rescinding' party's act in notifying the other party (for a qualification in the case of fraudulent misrepresentation by absconding rogues, see the text below on the *Caldwell* case (1965)) that he is setting aside or avoiding the contract, or proposes to do so. Alternatively, rescission can result from an order made by the court, at the innocent party's request: rescission then becomes a formal remedy issued

117 *Gran Gelato Ltd v. Richliff Group Ltd* [1992] Ch 560, 573–4, *per* Sir Donald Nicholls V-C (also noting that the 1945 Act requires section 2(1) liability to arise concurrently with liability for common law negligence on same facts).

118 *Ibid.*, at 574.

119 *Standard Chartered Bank v. Pakistan National Shipping Corporation (Nos. 2 and 4)* [2003] 1 AC 959, HL, at [18], *per* Lord Hoffmann, and [42] to [45], *per* Lord Rodger.

120 D. O'Sullivan, S. Elliott and R. Zakrewski, *The Law of Rescission* (Oxford, 2007), chapters 13 ff.

121 This distinction between void and voidable contracts continues to bedevil the contractual doctrine of mistake 'as to person' in English law: *Shogun Finance Ltd v. Hudson* [2003] UKHL 62; [2004] 1 AC 919, HL: see 10.23 ff.

by the court. Of these two modes of rescission, the first type, the extra-judicial ‘self-help method’, is much more common. This is because it conveniently involves merely private notification to the other party, without judicial intervention.¹²²

In the case of a fraudulent misrepresentation, the Court of Appeal in *Car & Universal Finance Co. v. Caldwell* (1965) held that the representee can rescind by notifying the world at large (for example, by notifying the police (10.35)).¹²³ It would be unreasonable to expect the representee to track down the elusive rogue in this situation. The court left open the question whether such indirect rescission (rescission, as it were, addressed to the world at large) should be effective where the misrepresentation was non-fraudulent or perhaps in other contexts of vitiated agreements (such as duress or undue influence).

- 9.19 *Indemnity in event of rescission.* Equity can impose an indemnity in favour of a party who has incurred expense during the currency of the transaction which is now rescinded. That party is entitled to such payment only in respect of expenditure necessarily incurred under the terms of the relevant transaction. A leading case is *Whittington v. Seale-Hayne* (1900).¹²⁴

In *Whittington v. Seale-Hayne* (1900), the defendant, before letting a poultry farm to the plaintiff tenant, had misstated it as in good condition. In fact, the buildings were in disrepair and it was in an insanitary state. The plaintiff succeeded in gaining rescission of the lease of the farm, and the court held that he could also recover the rent paid to the defendant, the rates paid to the rating authority, and the cost of repair work carried out pursuant to an order of the local authority. But the indemnity did not extend to the loss of pigs which had died as a result of the farm's insanitary state, nor to loss of profits from running the business, nor to medical expenses incurred by the manager who had also been rendered ill. Those claims in respect of loss without any corresponding ultimate gain to the misrepresenter would have required an action for compensation and hence proof of fraud (nowadays, such a claim for compensation would be made under section 2(1) of the Misrepresentation Act 1967, without proof of fraud, on the basis of the representer's statutory fault: on that provision, see 9.14 ff).

Commenting on this decision, McKendrick persuasively suggests:

[T]he reason for [the representee's] entitlement to recover these payments [in the *Whittington* case: see the passage above] was that they had resulted in an enrichment to the defendant (either through the direct payment of rent or by carrying out the work ordered by the local authority) and, when the lease was set aside, the defendant became subject to a restitutionary liability to repay to the plaintiff the value of the benefits which he had received as a result of the plaintiff's obligations [express or implied] under the lease.¹²⁵

122 J. O'Sullivan [2000] CLJ 509; a sophisticated critique of the proprietary aspects of rescission is S. Worthington, 'The Proprietary Consequences of Rescission' [2002] *Restitution Law Review* 28–69.

123 [1965] 1 QB 525, CA.

124 (1900) 82 LT 49; J. Cartwright, *Misrepresentation, Mistake and Non-Disclosure* (2nd edn, 2007), 417.

125 E. McKendrick, *Contract Law: Text, Cases and Materials* (4th edn, Oxford, 2010), 624.

9.20 *Bars to rescission.*¹²⁶ There are four general *judicial* bars. There is also a fifth, but *statutory*, bar restricted to non-fraudulent misrepresentation (see section 2(2) of the 1967 Act, 9.21). Any of these bars is sufficient to preclude rescission.

- (1) The right of rescission is lost or barred if *restoration is impossible*, that is, the parties can no longer be restored to their original position: *restitutio in integrum* has become impossible.¹²⁷
- (2) A *third party purchaser for value in good faith without notice* might have bought chattels, shares or land before the innocent party rescinded the contract; if so, rescission is barred.¹²⁸
- (3) The innocent party might have *affirmed* the contract and so lost the right to rescind.¹²⁹
- (4) There might have been a *substantial lapse of time* since the contract's formation, and, as a result of this lapse of time, rescission might no longer be just.¹³⁰

9.21 *Non-fraudulent misrepresentation: discretion to withhold rescission.* In the case of a *non-fraudulent* misrepresentation, the court possesses a *statutory* discretion to deny rescission when to withhold that remedy would be 'equitable' and instead to award damages 'in lieu' (either when the court, in its discretion, refuses rescission or, less often, if the court decides to reverse self-help rescission by the representee, *provided the representation was not fraudulent*). Section 2(2) of the Misrepresentation Act 1967 states:

Where a person has entered into a contract after a misrepresentation has been made to him otherwise than fraudulently, and he would be entitled, by reason of the misrepresentation, to rescind the contract, then, if it is claimed, in any proceedings arising out of the contract, that the contract ought to be or has been rescinded, the court or arbitrator may declare the contract subsisting and award damages in lieu of rescission, if of opinion that it would be equitable to do so, having regard to the nature of the misrepresentation and the loss that would be caused by it if the contract were upheld, as well as to the loss that rescission would cause to the other party.

Three points arise concerning this provision.

First, the better view is that section 2(2) presupposes that the right to rescind would otherwise subsist at the time the court considers whether to award 'damages in lieu';¹³¹ otherwise, the court lacks the power to award damages under this provision. The 'better

¹²⁶ *Chitty on Contracts* (30th edn, London, 2008), 6–115 ff.

¹²⁷ J. Cartwright, *Misrepresentation, Mistake and Non-Disclosure* (2nd edn, London, 2007), 4.08; *Chitty on Contracts* (30th edn, London, 2008), 6–116 ff.

¹²⁸ *Chitty on Contracts* (30th edn, London, 2008), 6–129.

¹²⁹ *Ibid.*, at 6–124.

¹³⁰ *Ibid.*, at 6–127.

¹³¹ *Ibid.*, at 6–098.

view', endorsed by *Chitty*,¹³² enjoys predominant judicial support¹³³ (admittedly, Jacob J took a different view).¹³⁴

Secondly, liability under section 2(2) does not require proof that the representor was in any way culpable.¹³⁵ By contrast, a representor is liable to pay damages *under section 2(1)* (9.14) only if he did not have reasonable grounds for believing the accuracy of his statement.

Thirdly, the nature of damages under section 2(2) is not clear. The better view is that damages under this provision concern the difference between the price paid and the actual value of the property:

The 'better view', just mentioned, is supported by *Chitty*,¹³⁶ *Treitel*¹³⁷ and *McGregor*.¹³⁸ They note that this measure is the pecuniary substitute for rescission, and this is normally assessed on the basis of the property's value at the time of the property's transfer, rather than including further loss resulting from a subsequent fall in the property's value,¹³⁹ although it is submitted that the court might choose a later date, if it was not practicable for the representee to have rescinded the contract at an earlier point.

Admittedly, some *dicta* (unattractively) suggest that section 2(2) might provide the 'cost of cure' measure of damages (on this concept, see 18.27),¹⁴⁰ or (again unattractively) that section 2(2) might remedy a claim for 'consequential loss'.¹⁴¹ But these statements are not authoritative.

8. TERMINATION FOR BREACH AND RESCISSION FOR MISREPRESENTATION CONTRASTED

9.22 'Rescission' is a technical word better applied to *rescission ab initio*, rather than 'termination for breach' (see also 17.49 ff). Thus, Lord Wilberforce in *Johnson v. Agnew* (1980), emphasising the need to distinguish between termination for breach and rescission for misrepresentation, said:¹⁴² 'In those cases [of rescission *ab initio*], the contract is treated

¹³² *Ibid.*

¹³³ *Atlantic Lines & Navigation Co. Inc. v. Hallam ('The Lucy')* [1983] 1 Lloyd's Rep 188, 202, Mustill J; *William Sindall plc v. Cambridgeshire County Council* [1994] 1 WLR 1016, 1044E, CA (Evans LJ, *dictum*); *Floods of Queensferry Ltd v. Shand Construction Ltd* [2000] BLR 81 (Judge Humphrey Lloyd QC); *Government of Zanzibar v. British Aerospace Ltd* [2000] 1 WLR 2333, 2341B–2344A, Judge Raymond Jack QC; noted by D. Malet, (2001) 117 LQR 524–8; J. O'Sullivan, [2001] CLJ 239; *Floods of Queensferry Ltd v. Shand Construction Ltd* [2000] BLR 81; *Pankhania v. Hackney London Borough Council* [2002] EWHC 2442 (Ch), at [77], Judge Rex Tedd QC.

¹³⁴ *Thomas Witter Ltd v. TBP Industries Ltd* [1996] 2 All ER 573, 590, Jacob J; noted by H. Beale, (1995) 111 LQR 385–8.

¹³⁵ *Government of Zanzibar v. British Aerospace Ltd* [2000] 1 WLR 2333, 2342C–E, Judge Raymond Jack QC.

¹³⁶ *Chitty on Contracts* (30th edn, London, 2008), 6–099; otherwise, the defendant would be unjustly enriched, as observed by P. Birks, [1997] *Restitution Law Review* 72, 75.

¹³⁷ *Treitel* (12th edn, London, 2007), 9–068.

¹³⁸ *McGregor on Damages* (18th edn, London, 2009), 41–062 to 41–070.

¹³⁹ As on facts of *William Sindall plc v. Cambridgeshire County Council* [1994] 1 WLR 1016, CA (where, however, no misrepresentation was established); *Chitty on Contracts* (30th edn, London, 2008), 6–101.

¹⁴⁰ *William Sindall plc v. Cambridgeshire County Council* [1994] 1 WLR 1016, CA, 1045–6, *per* Evans LJ in a *dictum*.

¹⁴¹ *Ibid.*; criticised in *Chitty on Contracts* (30th edn, London, 2008), 6–099 to 6–101.

¹⁴² [1980] AC 367, 392–3, HL, citing, notably, Lord Porter in *Heyman v. Darwins Ltd* [1942] AC 356, 399, HL, and Dixon J in *McDonald v. Denny Lascelles Ltd* (1933) 48 CLR 457, 476–7, High Court of Australia.

in law as never having come into existence ... [A]cceptance of a repudiatory breach does not bring about “rescission *ab initio*”.

9.23 The practical effects of this distinction are:

- (1) When a contract is terminated for breach, the innocent party retains the right to sue in respect of breaches of contract¹⁴³ or payment obligations¹⁴⁴ which antedate the termination.
- (2) The terminating party might himself remain liable in respect of his breaches of contract which antedated termination for the guilty party's breach.¹⁴⁵
- (3) Furthermore (see further 17.48), ancillary obligations will continue to apply, notably exclusion clauses (whether excluding liability or restricting liability), liquidated damages clauses, jurisdiction or arbitration clauses (for the survival of such clauses following rescission, see the remainder of this paragraph) and express repayment clauses (17.04).

Rescission *ab initio* does not destroy the contract utterly. This is certainly clear in the case of arbitration clauses: section 7 of the Arbitration Act 1996 treats an arbitration clause as an independent agreement, and as such it will survive the invalidity or disappearance of the main agreement. The Court of Appeal in *Mackender v. Feldia AG* (1967) held that rescission for non-disclosure by an insured did not annihilate a jurisdiction or exclusion clause.¹⁴⁶ It is submitted that other parts of a contract might also survive the process of rescission *ab initio*, if the court discerns a joint intention that the clause should govern the transaction, even if it proves voidable, such as liquidated damages clauses (in respect of misrepresentation) or exclusion clauses.

9.24 *Rescission precludes a claim to compensation for breach of contract.* Rescission *ab initio* removes the opportunity to bring a claim for contractual damages based on breach of an obligation contained in the contract. The reason for this is that rescission brings the contract to an end with retrospective effect. And so rescission removes the peg on which the claim for breach of contract might otherwise have hung. However, liability might sometimes arise under a collateral contract (9.05 to 9.10).

9.25 *Overlapping modes of ending the contract.* Section 1(a) of the Misrepresentation Act 1967 affirms that a representee can have alternative claims for misrepresentation and

¹⁴³ *Photo Production Ltd v. Securicor Transport Ltd* [1980] AC 827, 849, HL, *per* Lord Diplock; *Johnson v. Agnew* [1980] AC 367, 396, HL, *per* Lord Wilberforce; and see the decisions cited in the next note.

¹⁴⁴ *Hurst v. Bryk* [2002] 1 AC 185, HL (former partner liable for accrued and accruing rent liability for partnership premises when liability arose before one partner accepted the other partners' repudiatory breach); *Stocznia Gdanska SA v. Latvian SS Co.* [1998] 1 WLR 574, HL (liability to pay accrued instalments under contract for construction of a ship); *J. Beatson and G. Tolhurst*, [1998] CLJ 253).

¹⁴⁵ *Eastwood v. Magnox Electric plc* [2004] 1 All ER 991, HL, at [27].

¹⁴⁶ [1967] 2 QB 590, 603–4, CA, *per* Diplock LJ.

for breach of contract in respect of a pre-contractual false statement. Section 1 of the Misrepresentation Act 1967 states:

Where a person has entered into a contract after a misrepresentation has been made to him, and—

- (a) the misrepresentation has become a term of the contract; or
- (b) the contract has been performed;

or both, then, if otherwise he would be entitled to rescind the contract without alleging fraud, he shall be so entitled, subject to the provisions of this Act, notwithstanding the matters mentioned in paragraphs (a) and (b) of this section.

The representee must elect between rescission for misrepresentation and a contractual claim for breach of a term incorporated into the contract:¹⁴⁷

- (1) *Either*, he might elect to treat the misrepresentation *as a breach of a term in the contract* and sue for contractual damages; and he might terminate the contract for such breach if the term is a condition or, if the term is an innominate term, the breach is serious enough. Such termination for breach would entail prospective termination (on the scope for the innocent party to terminate for breach, see 17.09 and 17.18).
- (2) *Or* he might elect to disregard the ‘contractual term’ route just mentioned in (1) above, and instead *rescind ab initio* the contract by reason of misrepresentation. In addition to such rescission, he might also obtain damages for misrepresentation under section 2(1) of the Misrepresentation Act 1967, or in the tort of deceit. But an election to rescind *ab initio* for misrepresentation must analytically preclude an action for damages based upon breach of the term (9.23).

9. EXCLUSION CLAUSES AND THE MISREPRESENTATION ACT 1967¹⁴⁸

9.26 Section 3 of the Misrepresentation Act 1967 invalidates a clause which unreasonably excludes or restricts liability arising from a misrepresentation. This provision is applicable to all types of contract except contracts for the international supply of goods (this exception was noted by the Court of Appeal in *Trident Turboprop (Dublin) Ltd v. First Flight Couriers* (2009)).¹⁴⁹ Section 3 of the 1967 Act states:

If a contract contains a term which would exclude or restrict—

- (a) any liability to which a party to a contract may be subject by reason of any misrepresentation made by him before the contract was made; or

¹⁴⁷ Cheshire, Fifoot and Furmston’s *The Law of Contract* (15th edn, Oxford, 2007), 351, suggests that section 1 of the 1967 Act only applies where the representation reappears as a written term of the contract and not if it ‘occurs only once in the history of a transaction’.

¹⁴⁸ J. Cartwright, *Misrepresentation, Mistake and Non-Disclosure* (2nd edn, London, 2007), 9.18; J. Cartwright, in A. Burrows and E. Peel (eds.), *Contract Terms* (Oxford, 2007), chapter 11.

¹⁴⁹ [2009] EWCA Civ 290; [2010] QB 86, at [15] ff, *per* Moore-Bick LJ.

(b) any remedy available to another party to the contract by reason of such a misrepresentation,

that term shall be of no effect except in so far as it satisfies the requirement of reasonableness as stated in section 11(1) of the Unfair Contract Terms Act 1977; and it is for those claiming that the term satisfies that requirement to show that it does.

The Court of Appeal in *Cremdean Properties Ltd v. Nash* (1977) said that, if the reality is that a misrepresentation was made, section 3 of the 1967 Act cannot be evaded by clauses which purport to deny that fact.¹⁵⁰

However, the *Cremdean* case did not disturb the decision of Brightman J in *Overbrooke Estates v. Glencombe Properties Ltd* (1974), where the relevant clause denied that a party's agent had any authority to make statements affecting the principal.¹⁵¹ This clause was held not to be an exclusion clause. Therefore, section 3 of the 1967 Act did not apply.

Non-reliance clauses (9.28 ff) also require the court to consider the distinction between (1) a contractual provision purporting to preclude any possible 'misrepresentation' and (2) a clause which purports to cut back or exclude liability for a misrepresentation. On this distinction, Toulson J in *IFE Fund SA v. Goldman Sachs International* (2006)¹⁵² (whose judgment was upheld by the Court of Appeal in 2007)¹⁵³ lucidly commented:¹⁵⁴

The question is one of substance and not form. If a seller of a car said to a buyer 'I have serviced the car since it was new, it has had only one owner and the clock reading is accurate', those statements would be representations, and they would still have that character even if the seller added the words 'but those statements are not representations on which you can rely'. *Cremdean Properties Ltd v. Nash* ... is authority for the principle that a party cannot by a carefully chosen form of wording circumvent the statutory controls on exclusion of liability for a representation which has on proper analysis been made. If, however, the seller of the car said 'The clock reading is 20,000 miles, but I have no knowledge whether the reading is true or false', the position would be different, because the qualifying words could not fairly be regarded as an attempt to exclude liability for a false representation arising from the first half of the sentence.

In the present case Goldman Sachs supplied information obtained by it from other sources. The statements made by it in the [bonds purchase literature] regarding its non-verification of the accuracy or completeness of that information, and its non-acceptance of any responsibility for reviewing the information, went to the

150 (1977) 244 EG 547, CA; E. Peel, (2001) 117 LQR 545, 549, cites also *South Western General Property Co. Ltd v. Marton* (1982) 263 EG 1090 and *St Marylebone Property Co. Ltd v. Payne* [1994] EGLR 25.

151 [1974] 1 WLR 1335; [1974] 3 All ER 511, Brightman J; approved in *Museprime Properties Ltd v. Adhill Properties Ltd* (1990) 61 P & CR 111, CA.

152 [2006] EWHC 2887 (Comm); [2007] 1 Lloyd's Rep 264.

153 [2007] EWCA Civ 811; [2007] 2 Lloyd's Rep 449.

154 [2006] EWHC 2887 (Comm); [2007] 1 Lloyd's Rep 264, at [68] to [70].

scope of the representations being made and cannot properly be characterised for the purposes of [section 3 of the 1967 Act] as attempts to exclude liability for misrepresentation.

9.27 *Entire agreement clauses.* Such a clause states that the parties' contractual obligations are to be found only within the four corners of the written contract and not in any side or prior agreement.¹⁵⁵ Exclusion of collateral warranties in this manner does not fall within the scope of section 3 of the Misrepresentation Act 1967 (9.26) because that provision concerns only attempts to exclude or restrict liability for *misrepresentation* as distinct from contractual liability arising from breach of warranty.¹⁵⁶ As Lightman J said in the *Inntrepreneur* case (2000), 'an entire agreement provision does not preclude a claim in misrepresentation, for the denial of contractual force cannot affect the status of a statement as a misrepresentation.'¹⁵⁷ If a clause contained a provision which *purported to exclude or restrict liability for misrepresentations*, it would need to satisfy the test of reasonableness under section 3 of the 1967 Act.¹⁵⁸ Gloster J in the *Six Continents Hotels* case (2006) approved the following submission:¹⁵⁹ '[A]n entire agreement clause limits the terms of the parties' agreement to their written agreement and prevents a representation from assuming contractual force, but ... it does not, without more, preclude or exclude liability for misrepresentation.'

9.28 *Non-reliance clauses.* This type of clause involves the (potential) representee affirming that he has not relied on any representation other than those contained in the written agreement. The effect of this type of clause is to 'remove the rug' from under a representee's feet by excluding the element of reliance, even if it is not disputed that an inaccurate statement was made by the opponent. In *EA Grimstead & Son Ltd v. McGarrigan* (1999), Chadwick LJ¹⁶⁰ explained that such a clause precludes the representee from bringing a claim for (at any rate non-fraudulent) misrepresentation (9.31). As we shall see (9.30), the view now adopted is that a non-reliance clause operates as an 'estoppel by contract', precluding the representee from denying that he assured the other party that he had not relied on any possible representation.

9.29 *Non-consensual basis of non-reliance clauses: a view now rejected.* In the *Watford Electronics* case (2001), Chadwick LJ suggested that the clause operates as an instance of

155 *Deepak Fertilisers & Petrochemicals Corporation v. ICI Chemicals and Polymers Ltd* [1999] 1 Lloyd's Rep 387, 395, CA (noted by Gloster J in *Six Continents Hotels Inc. v. Event Hotels GmbH* [2006] EWHC 2317 (QB), at [49]).

156 *Inntrepreneur Pub Co. Ltd v. East Crown Ltd* [2000] 2 Lloyd's Rep 611, Lightman J, adopting *McGrath v. Shah* (1987) 57 P & CR 452 (Chadwick QC sitting as a Deputy High Court Judge).

157 *Inntrepreneur Pub Co. Ltd v. East Crown Ltd* [2000] 2 Lloyd's Rep 611, at [8].

158 *Ibid.*; and *Government of Zanzibar v. British Aerospace (Lancaster House) Ltd* [2000] 1 WLR 2333, 2344, Judge Raymond Jack QC.

159 *Six Continents Hotels Inc. v. Event Hotels GmbH* [2006] EWHC 2317 (QB), at [49], citing *Deepak Fertilisers v. ICI Chemicals* [1999] 1 Lloyd's Rep 387, 395, CA, *per* Stuart-Smith LJ; and *Witter v. TBP Industries Ltd* [1996] 2 All ER 573, 595, *per* Jacob J.

160 [1988–99] Info TLR 384, CA (CA, 27 October 1999; transcript No. 1733 of 1999).

estoppel by representation: B's assent to the clause indicates to A, who has inserted the clause, that A can assume that B is not relying on any misrepresentation.¹⁶¹

9.30 *Consensual basis of non-reliance clauses.* But, as Moore-Bick and Chadwick LJ suggested in the *Peekay* case (2006),¹⁶² a more attractive approach is to treat this estoppel as founded on 'estoppel by convention', the parties having conducted themselves in a way indicating agreement that the non-reliance clause will be honoured. And this view has been followed in more recent decisions: *JP Morgan Chase Bank v. Springwell Navigation Corp.* (2010)¹⁶³ and *Trident Turboprop (Dublin) Ltd v. First Flight Couriers* (2008)¹⁶⁴ (both decisions noted by Trukhtanov).¹⁶⁵ According to these decisions, because a non-reliance clause takes effect as a species of agreement, that is, 'estoppel by contract', there is no need to show that the representor has relied on the representee's assertion that the latter has taken no notice of (has 'not relied' on) any possible representation.

9.31 *Non-reliance clauses and statutory control.* Although there has been one instance of judicial doubt (Chadwick LJ in the *Watford Electronics* case (2001): see below), it is submitted that the better view is that a non-reliance clause does fall for consideration under the reasonableness test in section 3 of the Misrepresentation Act 1967. It will then be a question whether the clause survives the test of reasonableness (9.32).

In the *Watford Electronics* case (2001), Chadwick LJ denied that a 'non-reliance' clause would be caught by this provision. He said: 'It is true that an acknowledgement of non-reliance does not purport to prevent a party from proving that a representation was made, nor that it was false. What the acknowledgement seeks to do is to prevent the person to whom the representation was made from asserting that he relied on it.'¹⁶⁶

However, in an earlier case, the *Government of Zanzibar* case (2000), Judge Raymond Jack QC preferred the opposite view, namely, that a non-reliance clause does fall within the scope of section 3 of the 1967 Act.¹⁶⁷ Edwin Peel prefers the latter approach and attractively suggests that a non-reliance clause should, as a matter of substance, be

161 *Watford Electronics Ltd v. Sanderson CFL Ltd* [2001] EWCA Civ 317; [2001] 1 All ER (Comm) 696, at [38], [39], citing himself in *EA Grimstead & Son Ltd v. McGarrigan* [1988-99] Info TLR 384, CA (CA, 27 October 1999; transcript No. 1733 of 1999).

162 *Peekay Intermark Ltd v. Australia and New Zealand Banking Group Ltd* [2006] EWCA Civ 386; [2006] 2 Lloyd's Rep 511, at [56] and [57], Moore-Bick LJ, citing, as an example of such an estoppel, *Colchester Borough Council v. Smith* [1991] Ch 448, affirmed [1992] Ch 421, CA; (Chadwick LJ at [70] referred also to a 'contractual estoppel'); Moore-Bick LJ thought analysis by estoppel by representation an alternative possibility.

163 [2008] EWHC 1186, Gloster J, [556]; affirmed [2010] EWCA Civ 1221, at [171].

164 [2008] EWHC 1686; [2009] 1 All ER (Comm) 16, where this point is mentioned by Aikens J in a footnote (n. 9) expressly approving Gloster J's analysis in the *Springwell* case (see the preceding footnote). Aikens J's decision was affirmed on appeal without discussion of the point, [2009] EWCA Civ 290; [2010] QB 86.

165 A. Trukhtanov, (2009) 125 LQR 648.

166 *Watford Electronics Ltd v. Sanderson CFL Ltd* [2001] EWCA Civ 317; [2001] 1 All ER (Comm) 696, at [40]; criticised by E. Peel, (2001) 117 LQR 545, 548-9, *Treitel* (12th edn, London, 2007), 9-114 n. 526, and J. Cartwright, in A. Burrows and E. Peel (eds.), *Contract Terms* (Oxford, 2007), 213, at 222-5.

167 *Government of Zanzibar v. British Aerospace (Lancaster House) Ltd* [2000] 1 WLR 2333, 2347H-2348, Judge Raymond Jack QC.

regarded as within section 3 of the 1967 Act.¹⁶⁸ Peel says: '[If section 3 were not to apply] this would leave the court with no opportunity to police such clauses when they are used against consumers, or parties of unequal bargaining power. A [gap] in the drafting of the legislation would have been allowed to undermine its clearly intended effect. This can, and should, be avoided by the courts.' In a short comment, Aikens J in *Trident Turboprop (Dublin) Ltd v. First Flight Couriers* (2008)¹⁶⁹ expressed support for the 'logic' of Chadwick LJ's approach, but then found on the facts of that case that the relevant clause did purport to exclude or restrict liability for a purported representation.

It is submitted that Peel's approach is more attractive. Chadwick LJ's unwillingness in the *Watford Electronics* case (2001) to apply the statutory reasonableness provision to non-reliance clauses is a logician's approach. It is unattractive because it would too often enable undeserving representors to escape liability without first having to satisfy the reasonableness test of section 3 of the 1967 Act. Moreover, pushed to its extreme limits, Chadwick LJ's analytical approach would even justify declaring that a fraudulent misrepresentation was not operative because the representee had acknowledged that he had not relied on it.

It is submitted, therefore, that (1) in the case of a non-fraudulent misrepresentation, a non-reliance clause should fall within the 'reasonableness' test of section 3 of the 1967 Act; and (2) in the case of a fraudulent misrepresentation, the common law rule forbidding exclusion or limitation of liability (9.33 and proposition (1) at 15.01) should prevent a representor from asserting a non-reliance clause as a counter to the usual inference that the statement influenced the representee¹⁷⁰ (although it should still be possible for the fraudulent representor in this context to escape liability if he can show (a) that the representee was unaware of the fraudulent statement or (b) that, even if aware, the representee clearly chose not to be influenced at all by that statement).

- 9.32 Finally, if section 3 of the 1967 Act were to apply to a non-reliance clause, how would the question of statutory 'reasonableness' be approached? The following points emerge from Gloster J's *dicta* in the *Six Continents Hotels* case (2006) on this issue:¹⁷¹ (1) the court should recall that a non-reliance clause (like an entire agreement clause) is designed to avoid disputes concerning matters not contained in the written agreement; (2) the risks contained in the written document are reflected in the overall price and structuring of the transaction; (3) it will be especially relevant whether the agreement was 'sophisticated' and the result of negotiations conducted by legal advisors; and (4) it will be relevant whether the agreement was made between parties of roughly equal bargaining power (on this last point, see also the *Springwell* case (2008), cited at 15.24).

168 [2001] 117 LQR 545, 549 (case note on the *Watford Electronics* case).

169 [2008] EWHC 1686; [2009] 1 All ER (Comm) 16, at [48] (this point was not considered on appeal: [2009] EWCA Civ 290; [2010] QB 86).

170 As supported by *dicta* of Gloster J in *Six Continents Hotels Inc. v. Event Hotels GmbH* [2006] EWHC 2317 (QB), at [53].

171 *Six Continents Hotels Inc. v. Event Hotels GmbH* [2006] EWHC 2317 (QB), at [54] and [55]; citing extensively from Chadwick LJ in *Grimstead & Son Ltd v. McGarrigan* [1988–99] Info TLR 384, CA (CA, 27 October 1999; transcript No. 1733 of 1999), especially for points (1) and (2) summarised in text above.

9.33 *Potential liability for fraud.* The common law prevents a party from excluding or limiting liability for fraudulent misstatements. A clause which is literally wide enough to include a fraudulent statement will be construed as not extending to fraud, by virtue of this common law rule. This will leave intact the non-fraudulent element of the clause (liability for negligent misrepresentation, at common law or under section 2(1) of the 1967 Act), and that element can be subjected to the statutory test of reasonableness contained in section 3 of the 1967 Act. Gloster J adopted this approach in the *Six Continents Hotels* (2006) case.¹⁷² Her attractive analysis is consistent with Judge Jack QC's view in the *Government of Zanzibar* case (2000)¹⁷³ (but Gloster J explicitly rejected Jacob J's view in *Thomas Witter Ltd v. TBP Industries Ltd* (1996),¹⁷⁴ where Jacob J held that, if an exclusion clause is literally wide enough to include fraud, then the clause is bound to fail in its entirety under section 3 of the 1967 Act, unless its 'non-fraudulent' element can be severed from its 'fraudulent' element). Gloster J said in the *Six Continents Hotels* case (2006):¹⁷⁵

In *Government of Zanzibar v. British Aerospace Ltd* (2000) His Honour Judge Raymond Jack QC, sitting as a High Court Judge, did not follow the approach of Jacob J in *Witter* (1996) [and instead Judge Jack] held that since long standing authority, such as *S Pearson & Son Ltd v. Dublin Corporation* [1907] AC 351, clearly established that such clauses excluding or limiting liability were not apt on their true construction to cover fraudulent misrepresentation, section 3 (of the 1967 Act) could (on the facts) have no application [to such attempted exclusion]. [Judge Jack] also referred to the unreported Court of Appeal case of *Grimstead & Son Ltd v. McGarrigan* (1999)¹⁷⁶ where ... [a]lthough the Court did not expressly address the point made by Jacob J, its decision on the reasonableness issue under section 3 of the 1967 Act appears to be inconsistent with his approach.

10. DUTIES TO DISCLOSE¹⁷⁷

9.34 The starting point is the general proposition that a party to pre-contractual negotiations is under no duty to disabuse the other of an error concerning the quality, nature or utility

¹⁷² *Six Continents Hotels* case, [2006] EWHC 2317 (QB), [53].

¹⁷³ *Government of Zanzibar v. British Aerospace Ltd* [2000] 1 WLR 2333, 2344A–2348A.

¹⁷⁴ [1996] 2 All ER 573, 597–8, Jacob J; noted by H. Beale (1995) 111 LQR 385, 388–9.

¹⁷⁵ *Six Continents Hotels* case, [2006] EWHC 2317 (QB), [53].

¹⁷⁶ *Grimstead & Son Ltd v. McGarrigan* [1988–99] Info TLR 384, CA (CA, 27 October 1999; transcript No. 1733 of 1999).

¹⁷⁷ J. Cartwright, *Misrepresentation, Mistake and Non-Disclosure* (2nd edn, London, 2007), chapters 16 and 17; Chitty on Contracts (30th edn, London, 2008), 6.142 ff; D. O'Sullivan, S. Elliott and R. Zakrzewski, *The Law of Rescission* (Oxford, 2008), chapter 5; Spencer Bower, Turner and Sutton: *Actionable Non-Disclosure* (2nd edn, London, 1990); PECL, *Principles of European Contract Law*, Article, 4:107 and UNIDROIT's *Principles of International Commercial Contracts*, Article 3.8, render a contract voidable if there is *fraudulent* non-disclosure of 'circumstances' or 'information', which failure conflicts with 'reasonable commercial standards of fair dealing' (UNIDROIT) or 'good faith and fair dealing' (PECL); PECL, Article 4:107(3), specifies various additional factors; on the UNIDROIT principle, see M. J. Bonell (ed.), *The UNIDROIT Principles in Practice: Case Law and Bibliography on the UNIDROIT Principles of International Commercial Contracts* (2nd edn, Ardsley, NY, 2006), 203 ff; S. Vogenauer

of the transaction's subject matter stated (3.65 to 3.70; 10.16 and 10.17). This proposition was stated in *Smith v. Hughes* (1871).¹⁷⁸ The same proposition was affirmed, first, by Lord Atkin in *Bell v. Lever Bros Ltd* (1932),¹⁷⁹ and, secondly, by Lord Hoffmann in the *BCCI* case (2002),¹⁸⁰ where he commented: [T]here is obviously room in the dealings of the market for legitimately taking advantage of the known ignorance of the other party.' However, it would be wrong to suppose that a party to negotiations can always refrain from pointing out errors or otherwise engage in artful silence. The following qualifications or exceptions must be noted:

- (1) *Half-truths*. A pre-contractual statement might involve a misrepresentation because it discloses only part of the true position and conveys a false position regarding the whole situation. The true view is that such a misleading positive statement is a misrepresentation and so can give rise to liability in damages. Such a positive claim was not, however, necessary on the facts of *Curtis v. Chemical Cleaning and Dyeing Co.* (1951). The defendant dry-cleaning company told the plaintiff that an exclusion clause which she was about to sign covered loss due only to damage to beads and sequins; but in fact it covered all forms of damage, including, on the facts, a stain caused during the cleaning process; because of this misleading statement, the defendant was precluded from relying on the exclusion clause in these circumstances;¹⁸¹
- (2) *Misleading conduct*. Deliberate steps taken by B to conceal from A the true state of affairs can constitute misrepresentation by conduct: for examples, see the discussion under heading (1) at 9.02, noting *Spice Girls Ltd v. Aprilia World Service BV* (2002),¹⁸² and *Gordon v. Selico* (1986);¹⁸³ as the latter case shows, the active nature of this conduct can produce liability in damages.
- (3) *Falsification known to representor before contract formed*. A will have the right to rescind a contract if B has made an initially accurate statement but, before the contract's formation, B discovers a change of situation rendering that statement misleading and B fails to notify this change to A. Furthermore, B's failure to discover the change can sometimes involve an absence of 'reasonable grounds' for maintaining that statement and so expose B to liability to pay compensation under section 2(1) of the 1967 Act (on both aspects, see 9.03).

and J. Kleinheisterkamp (eds.), *Commentary on the UNIDROIT Principles of International Commercial Contracts* (Oxford, 2009), 434 ff; for comparative law discussion, see B. Nicholas, in D. R. Harris and D. Tallon (eds.), *Contract Law Today* (Oxford, 1989), 166–87; on the position in French law, see J. Ghestin, in Harris and Tallon, *ibid.*; and M. Fabre-Magnan, in J. Beatson and D. Friedmann (eds.), *Good Faith and Fault in Contract Law* (Oxford, 1995), chapter 4.

178 (1871) LR 6 QB 597.

179 [1932] AC 161, 224, HL.

180 *BCCI v. Ali* [2002] 1 AC 251, HL, at [70].

181 [1951] 1 KB 805, 810, CA, *per* Denning LJ.

182 [2002] EWCA Civ 15; [2002] EMLR 27; *Chitty on Contracts* (30th edn, London, 2008), 6–011, 6–015.

183 (1986) 18 HLR 219, CA (dry rot; defects deliberately covered up in flat; liability for deceit); similarly, *Schneider v. Heath* (1813) 3 Camp 505; 170 ER 1462 (ship kept afloat to conceal defective bottom and broken keel; active misrepresentation).

- (4) *Mistake as to terms of deal: other party acquiescing.* If B knows that A is mistaken regarding B's identity (10.36 to 10.40) or as to the terms of the proposed transaction (*Hartog v. Colin & Shields* (1939)¹⁸⁴ (3.65)), the contract cannot be upheld by B. In such a case, either the contract is void and/or (in the case of error as to terms) A might also have the right to insist that the contract proceed on A's supposed version (see the last portion of 3.66).
- (5) *Insurance.* Both an insurer and an assured (likewise, a reinsurer and a reassured) are obliged to disclose material facts concerning the proposed transaction.¹⁸⁵ In this 'insurance' or 'reinsurance' context, a failure to disclose does not give the 'victim' a right to compensation; instead, it gives him merely a right to rescind the transaction (on rescission, see 9.18). This proposition is supported by Court of Appeal¹⁸⁶ and House of Lords¹⁸⁷ authority. More generally, leading textbook writers¹⁸⁸ have disapproved the unreasoned attempt, in *Conlon v. Simms* (2006), by Lawrence Collins J and, on appeal, by Jonathan Parker LJ,¹⁸⁹ to build a ground of liability for damages from a mere failure to disclose, even if that failure is characterised as fraudulent and even if there is a positive duty to disclose arising from the relationship between the parties, as in the case of prospective partners. As for the question of inducement and reliance upon non-disclosure in the insurance context, Clarke LJ in *Assicurazioni Generali SpA v. Arab Insurance Group (BSC)* (2002) summarised the relevant factors¹⁹⁰ (see the passage cited at 9.04 at (3) above).
- (6) *Creditor and guarantees.* A creditor is obliged to reveal circumstances which directly affect the nature of the transaction for which the guarantor is about to act as surety, but this duty of disclosure has been circumscribed in the cases.¹⁹¹

184 [1939] 3 All ER 566, Singleton J.

185 *Pan Atlantic Insurance Co. Ltd v. Pine Top Insurance Co. Ltd* [1995] 1 AC 501, HL applied and considered in *St Paul Fire & Marine Insurance Co. (UK) Ltd v. McConnell Dowell Constructors Ltd* [1996] 1 All ER 96, CA; and *Assicurazioni Generali SpA v. Arab Insurance Group (BSC)* [2002] EWCA Civ 1642; [2003] 1 All ER (Comm) 140; [2003] 2 CLC 242.

186 *Banque Keyser Ullmann SA v. Skandia (UK) Insurance Co. Ltd* [1980] 1 QB 665, 774–81, CA, per Slade LJ, giving the court's judgment.

187 *Banque Keyser Ullmann SA v. Skandia (UK) Insurance Co. Ltd* [1991] 2 AC 249, 280, HL (Lord Templeman, endorsing Slade LJ's judgment, see the previous footnote); and *Manifest Shipping Co. v. Uni-Polaris Insurance Co. ('The Star Sea')* [2001] UKHL 1; [2003] 1 AC 469, at [46], per Lord Hobhouse.

188 *Anson's Law of Contract* (29th edn, Oxford, 2010), 342–3; J. Cartwright, 'Liability in Tort for Pre-Contractual Non-Disclosure', in A. Burrows and E. Peel (eds.), *Contract Formation and Parties* (Oxford, 2010), 137, at 147–9; J. Cartwright, *Misrepresentation, Mistake and Non-Disclosure* (2nd edn, London, 2007), 17.36 nn. 46–7; *Chitty on Contracts* (30th edn, London, 2008), 6.143; *Treitel* (12th edn, London, 2007), 9.150 n. 681.

189 [2006] EWHC 401; [2006] 2 All ER 1024, at [202], and supported by Jonathan Parker LJ on appeal, [2006] EWCA Civ 1749; [2008] 1 WLR 484, at [130]. Neither judge cites supporting case law authority, so the point is mere assertion.

190 [2002] EWCA Civ 1642; [2003] 1 All ER (Comm) 140; [2003] 2 CLC 242, at [62].

191 *Levett v. Barclays Bank plc* [1995] 1 WLR 1260 (Burton QC, Deputy High Court Judge, applying *Hamilton v. Watson* (1845) 12 C & F 109, HL); *Crédit Lyonnais Bank Nederland v. Export Credit Guarantee Department* [1996] 1 Lloyd's Rep 200, 227, Longmore J (emphasising the narrow scope of this duty); generally, see G. Andrews and R. Millett, *The Law of Guarantees* (5th edn, London, 2008); J. O'Donovan and J. Phillips, *The Modern Contract of Guarantee* (2nd edn, London, 2010).

- (7) *Fiduciaries*. A duty to disclose¹⁹² can arise in negotiations between a principal and his fiduciary, so that the latter is obliged to speak out.¹⁹³
- (8) *Relationships of 'trust and confidence' under the rubric of undue influence*. The Court of Appeal in *Hewett v. First Plus Financial Group* (2010)¹⁹⁴ (11.28, 11.31) held that a proven relationship of trust and confidence between husband and wife can import a duty to refrain from deliberate suppression of a material fact, such as non-disclosure of the fact that the husband was having an affair with another person.
- (9) *Rectification*. The equitable remedy of rectification can be ordered in A's favour where, during the negotiations, B has perceived that A is mistaken concerning the terms of the proposed transaction but has unconscionably remained silent, allowing the final written terms to be concluded in a manner which contradicts A's assumption (14.43 ff).

192 E.g. partners, *Conlon v. Simms* [2006] EWCA Civ 1749; [2008] 1 WLR 484; J. Cartwright, *Misrepresentation, Mistake and Non-Disclosure* (2nd edn, London, 2007), 17.19 and 17.33 to 17.35.

193 *Calvert v. William Hill Credit Ltd* [2008] EWCA Civ 1427; [2009] Ch 330, at [53]; *Parker and Mellows: The Modern Law of Trusts* (9th edn, London, 2008), 10-048 ff; J. Edelman, 'When Do Fiduciary Duties Arise?' (2010) 126 LQR 302.

194 *Hewett v. First Plus Financial Group* [2010] EWCA Civ 312; [2010] Fam Law 589, adopting David Richards J's statement in *Royal Bank of Scotland v. Chandra* [2010] EWHC 105 (Ch): '[D]eliberate suppression of information because the husband knows that, if disclosed, it will deter the wife from giving the guarantee, will involve an abuse by him of her confidence. It would be unconscionable and rightly categorised as unacceptable means.'

Chapter contents

1. Introduction *para.* 10.01
2. The nature of mistake *para.* 10.02
3. Shared mistake at common law *para.* 10.06
4. No rescission for shared mistake in equity: '*The Great Peace*' repudiating *Solle v. Butcher* *para.* 10.12
5. Unilateral error concerning subject matter *para.* 10.16
6. Denial of specific performance *para.* 10.18
7. '*Non est factum*': fundamental error in signed documents *para.* 10.20
8. Deeds and 'voluntary instruments' voidable in equity *para.* 10.22
9. Mistake concerning a party's identity *para.* 10.23

10

Mistake

1. INTRODUCTION¹

10.01 Summary of main points

- (1) The starting point (which is an expression of the objective principle of agreement: 3.57 ff) is that a contract is valid if party A alone is mistaken as to the nature or some aspect of the proposed contract; that is, party B did not induce A's error, nor did B unconscionably acquiesce in that error. This proposition is normally expressed by saying that 'unilateral' error does not vitiate a contract, that is, it does not count (for qualifications, see (2) immediately below).
- (2) Unilateral error (on which see (1) above) becomes relevant (the error becomes 'operative', to use the jargon of this topic) only in one of the following three situations:
 - (a) if B did not speak out to disabuse A of his error when B had been aware of A's error *as to the existence or meaning of an oral or written term*: A's mistake becomes 'operative',² enabling A *at common law* to be excused from performing the supposed agreement; or
 - (b) in the case of written contracts, A can *obtain rectification* of the agreement, so that A's 'version' of it is incorporated into the final text (14.33 ff), if B is aware of A's error concerning the terms of the final form of the document but B fails to disabuse A of this error; or
 - (c) a unilateral error can also justify 'refusal of specific performance' (an *equitable* remedy, 18.14)³ if B is aware of the other's error but fails to disabuse A of this error.

¹ Generally on the history of mistake doctrine, see C. MacMillan, *Mistakes in Contract Law* (Oxford, 2010); on the nineteenth century, see M. Lobban, in W. Cornish, J. S. Anderson, R. Cocks, M. Lobban, P. Polden and K. Smith, *The Oxford History of the Laws of England*, vol. XII, 1820–1914: *Private Law* (Oxford, 2010), 433 ff.

² A unilateral error concerning the subject matter is not enough: there is a need for A to be aware of B's error as to terms: *Smith v. Hughes* (1871) LR 6 QB 597; A. W. B. Simpson, (1975) 91 LQR 247, 265–9.

³ *Tamplin v. James* (1880) 15 Ch D 215, CA.

- (3) 'Common mistake' applies where the parties to a supposed agreement share a 'fundamental' error which deprives one party (or both) of the benefits which she tried to obtain from the agreement: see, for example, *Bell v. Lever Bros Ltd* (1932)⁴ and '*The Great Peace*' (2002).⁵ In both cases, this test was not satisfied on the facts.
- (4) '*The Great Peace*' (2002)⁶ formulated this narrow test for shared mistake at common law: whether the true circumstances differ radically from the supposed contractual arrangement, to the extent that it is 'impossible' to satisfy that expected performance. However, the 'impossibility' requirement is too strict and will need to be softened;⁷ and this requirement is probably inconsistent with the speeches in *Bell v. Lever Bros Ltd* (1932), which contemplate a wider test of 'fundamental difference'.
- (5) Common mistake will not arise if the relevant matter (for example, pre-contractual destruction or impairment of the subject matter) was subject to an express or implied term, or a risk assumed by one party.
- (6) '*The Great Peace*' (2002)⁸ repudiates the slender line of cases associated with *Solle v. Butcher* (1950), which had espoused an equitable doctrine of shared mistake.⁹
- (7) Error as to a party's identity is another category of mistake (6.61 ff). The leading discussion is now *Shogun Finance v. Hudson* (2004).¹⁰ 'Identity error' normally concerns a party's fraudulent impersonation. The source of this vexatious 'mistake' problem is that a rogue, X, pretending to be Y, dupes C into selling goods to X, and X then sells the same goods to D, the sub-purchaser, who buys them in good faith. X absconds and falls out of the picture. The law has a choice between two analyses: that D has acquired good title from X (the latter having received a voidable title when he dealt with C); or that C remains owner because X had derived no title from C, and so X had no title to transfer to D (under the principle of *nemo dat quod non habet*, D is unprotected if X lacked even a voidable title). Thus, a sub-purchaser is unprotected if the main 'contract' between head vendor and rogue was void *ab initio*. However, if the contract is voidable, the sub-vendor can acquire good title if he bought the relevant chattel from the rogue in good faith and before the head vendor had rescinded the contract (on the nature of rescission, see 9.18). *Shogun Finance v. Hudson* (2004) supports

4 [1932] AC 161, HL, notably Lord Atkin at 217–27 and Lord Thankerton at 233–6; and see Lord Blanesburgh at 181, middle paragraph.

5 *Great Peace Shipping Ltd v. Tsaviris Salvage (International) Ltd* [2002] EWCA Civ 1407; [2003] QB 679; noted by F. M. B. Reynolds, (2003) 119 LQR 177; and by S. Midwinter, (2003) 119 LQR 180.

6 *Ibid.*

7 Cf Sedley LJ in *Brennan v. Bolt Burdon* [2004] EWCA Civ 1017; [2005] QB 303, at [60]: 'I think that in cases of mutual mistake of law a different test may be necessary.'

8 *Great Peace* case, [2003] QB 679, CA.

9 *Ibid.*, not following *Solle v. Butcher* [1950] 1 KB 671, CA.

10 *Shogun Finance Ltd v. Hudson* [2004] 1 AC 919, HL, *per* Lords Hobhouse, Phillips and Walker.

three propositions: (a) that face-to-face transactions are unlikely to be regarded as void for error as to person, and instead will normally be voidable; this is because one party usually intends to deal with the other who is physically opposite, and the error concerns that person's good faith and creditworthiness, as *Lewis v. Averay* (1972) indicates;¹¹ (b) however, there is a chance that dealings between persons who are not face-to-face might involve a void contract, as in *Cundy v. Lindsay* (1878);¹² (c) the identity of parties to a written agreement is established by the names stated in that agreement.¹³

- (8) The main survivor of 'The Great Peace' case's¹⁴ assault on 'mistake' in equity is the doctrine of *rectification*; that doctrine permits the court to rewrite a documentary agreement to reflect the parties' prior consensus.¹⁵ Rectification is discussed at 14.33.

General

D. Friedmann, 'The Objective Principle and Mistake ...' (2003) 119 LQR 68, especially 68–84

C. MacMillan, *Mistakes in Contract Law* (Oxford, 2010)

J. Cartwright, *Misrepresentation, Mistake and Non-Disclosure* (2nd edn, London, 2007)

Bell v. Lever Bros Ltd

C. MacMillan, 'How Temptation Led to Mistake: An Explanation of Bell v. Lever Brothers, Limited' (2003) 119 LQR 625 (especially concerning the three stages of this litigation: Wright J at first instance, [1931] 1 KB 557, 567 (MacMillan, *ibid.*, 646–9); the Court of Appeal, [1931] 1 KB 588–600 (MacMillan, *ibid.*, 649–50); and the House of Lords, [1932] AC 161 (MacMillan, *ibid.*, 650–9))

'The Great Peace'

F. M. B. Reynolds, (2003) 119 LQR 177

S. Midwinter, (2003) 119 LQR 180

K. F. K. Low, 'Coming to Terms with The Great Peace in Common Mistake', in J. W. Neyers, R. Bronaugh and S. G. A. Pitel (eds.), *Exploring Contract Law* (Oxford, 2009), 319 ff

11 [1972] 1 QB 198, CA (approved in *Shogun* [2004] 1 AC 919, HL).

12 (1878) 3 App Cas 459, HL (upheld by majority in *Shogun* [2004] 1 AC 919, HL).

13 Upholding Dyson and Brooke LJJ in the Court of Appeal below; and applying *Hector v. Lyons* (1988) 58 P & CR 156, CA, at 158–9, 160.

14 [2003] QB 679, CA.

15 *Rose (Frederick E) (London) Ltd v. Wm H Pim Jr & Co. Ltd* [1953] 2 QB 450, CA; *Joscelyne v. Nissen* [1970] 2 QB 86, CA; *Riverlate Properties v. Paul* [1975] Ch 133, CA; *Commission for New Towns v. Cooper (GB) Ltd* [1995] Ch 259, CA.

Solle v. Butcher

- C. MacMillan, in C. Mitchell and P. Mitchell (eds.), *Landmark Cases in the Law of Restitution* (Oxford, 2006)
- J. Cartwright, 'Solle v. Butcher and the Doctrine of Mistake in Contract' (1987) 103 LQR 594
- A. Phang (1989) LS 291 (for an argument that common law and equitable doctrines of mistake should have been fused)

Pre-'The Great Peace' literature

- J. C. Smith, 'Contracts – Mistake, Frustration and Implied Terms' (1994) 110 LQR 400 (radical criticism of the doctrine of mistake)
- C. J. Slade, 'The Myth of Mistake in the English Law of Contract' (1954) 70 LQR 386 (for earlier criticism along same lines as Smith)

Void contracts and mistake as to identity

- D. W. McLaughlan, 'Parol Evidence and Contract Formation' (2005) 121 LQR 9
- C. MacMillan, 'Mistake as to Identity Clarified?' (120) LQR 368
- A. Phang, P.-W. Lee and P. Koh, 'Mistaken Identity in the House of Lords' [2004] CLJ 24
- R. Stevens, 'Objectivity, Mistake and the Parol Evidence Rule', in A. Burrows and E. Peel (eds.), *Contract Terms* (Oxford, 2007), chapter 6, at 110 ff
- Law Reform Committee, *Transfer of Title to Chattels* (Twelfth Report of the Law Reform Committee, Cmnd 2958, 1966)

2. THE NATURE OF MISTAKE¹⁶

- 10.02 *Need for apparent agreement.* A 'mistake' only becomes an issue if, first, there is an outward appearance of an agreement, that is, a consensus which is 'objectively discernible' (on this, see Lord Millett in the *Shogun* case).¹⁷ No such outward appearance of accord can be identified if A and B have exchanged offers which relate to manifestly different subject matters, or ambiguously described subject matters.¹⁸ A further step was taken in *Raffles v. Wichelhaus* (1864) where an apparent agreement, on closer inspection of the facts, turned out to be no real accord at all (for details of the case, see 4.10).¹⁹

16 D. Friedmann, (2003) 119 LQR 68–85 (thereafter dealing with mistake and restitutionary claims); pre-*Great Peace* literature: J. C. Smith, (1994) 110 LQR 400–19 (radical criticism of common mistake doctrine); earlier criticism along the same lines: C. J. Slade, 'The Myth of Mistake ...' (1954) 70 LQR 386; J. Cartwright, (1987) 103 LQR 594; A. Phang, (1989) LS 291.

17 *Shogun Finance Ltd v. Hudson* [2003] UKHL 62; [2004] 1 AC 919, HL, at [81] (especially second sentence), [82].

18 E.g. *Falck v. Williams* [1900] AC 176, PC.

19 (1864) 2 H & C 906; G. Gilmore, *The Death of Contract* (Columbus, OH, 1974), 35 ff; A. W. B. Simpson, *Leading Cases in the Common Law* (Oxford, 1995), 135 ff; C. MacMillan, *Mistakes in Contract Law* (Oxford, 2010), 186 ff; on this 1864 decision, see '*The Great Peace*' [2003] QB 679, CA, at [28] and [29].

10.03 *Types of mistake.* ‘Mistake’ becomes relevant in contract law in three main situations:

- (1) *Induced mistake.* If D makes a material misrepresentation on which P relies, P can claim (a) rescission for misrepresentation and, whether in the alternative or in addition, P can plead (b) that the misrepresentation entitles P to damages at common law or under section 2(1) of the Misrepresentation Act 1967 (the damages claim under the 1967 Act is more attractive: see 9.14 to 9.17). Misrepresentation, a major part of contract law, receives detailed discussion in chapter 9.
- (2) *Shared or common mistake.* D and P are mistaken jointly (they ‘share’ the mistake) about some essential feature of the subject matter of the contract. Before ‘*The Great Peace*’ (2002), it was considered that, both at common law and in equity, there were doctrines applicable to this situation (see below).²⁰ But, as will be shown, after ‘*The Great Peace*’, only the common law applies to a shared mistake, and equity no longer applies to that type of mistake.
- (3) *Unilateral mistake known to the other party.* There are two possibilities. First, D is aware of P’s error as to terms and fails to disabuse P of this mistake.²¹ Secondly, there is an error as to person: P makes an offer to D, P being mistaken as to D’s identity (attributes will not do), and D, usually a rogue, purports to accept P’s offer.

10.04 *Narrow doctrine.* Mistake in pure form is a residual ground. The tendency in recent decades has been to treat this as a narrow doctrine, subject to the following two main constraining factors:²² first, the parties’ allocation of risks, express or otherwise, will normally prevent a plea of mistake from succeeding; secondly, the courts have adopted a strict approach when applying the concept of ‘fundamental mistake’ at common law. Thus, attempts to invoke the doctrine of mistake in the context of commercial agreements have been largely unsuccessful.²³

10.05 *Mistake and related doctrines.* Suppose A sells a picture to B for £5m. The picture is believed by both to be a Picasso. This situation gives rise to five possible permutations:

- (1) *Breach of contract.* B can return the picture, or sue for damages, if it was a term of the contract that ‘it is a Picasso’.²⁴

20 Common law: e.g. *Smith v. Hughes* (1871) LR 6 QBD 597; *Bell v. Lever Bros Ltd* [1932] AC 161; *Hartog v. Colin and Shields* [1939] 3 All ER 566; *OT Africa v. Vickers plc* [1996] 1 Lloyd’s Rep 700, Mance J. Equity: *Solle v. Butcher* [1950] 1 KB 671, CA (see further 10.12 ff).

21 *OT Africa v. Vickers* [1996] 1 Lloyd’s Rep 700, 703, Mance J (‘knowledge’ includes imputed knowledge, that is, ‘a mistake by one party’ which ‘the other knew or ought reasonably to have known’, in other words, an obvious error which the non-mistaken party ought to have appreciated: see 10.17 and 3.65).

22 D. Friedmann, (2003) 119 LQR 68–85 (thereafter dealing with mistake and restitutionary claims).

23 E.g. *Clarion Ltd v. National Provident Institution* [2000] 1 WLR 1888, Rimer J.

24 *Harlingdon & Leinster Enterprises Ltd v. Christopher Hull Fine Art* [1990] 1 All ER 337, CA; noted by [1990] LMCLQ 455: see 9.06.

- (2) *Misrepresentation*. B can rescind the contract (even if the misrepresentation was not culpable) (and obtain damages if the misrepresentation has been culpable) if A has made a misrepresentation in stating that it is a Picasso.²⁵
- (3) *Property already owned by purchaser/property destroyed before sale*.²⁶ The contract is void if the painting sold to B was in fact already B's property.²⁷ The same is true if the picture is destroyed before the sale through no fault of the vendor.²⁸
- (4) *Shared error as to 'quality'*. However, mistake in this context is rightly described by Treitel as implausible because the contract is likely to contain an express term concerning the painting's authenticity, or the speculative and risk-laden nature of the contract will exclude mistake by allocating the risk or 'gamble' to one of the parties, depending on whether the price was set at a high or a low level. The question arises: what if A and B spontaneously believed that the picture was a Picasso, but it was by someone else? A *dictum* in Lord Atkin's speech in *Bell v. Lever Bros Ltd* (1932), concerning paintings, indicates that the agreement is nevertheless a valid agreement.²⁹ This is because of the narrow nature of fundamental error at common law. Until 2002, a more generous test, enunciated in *Solle v. Butcher* (equity's leading, but controversial, case) potentially enabled B to rescind the contract on the basis of a 'fundamental' error shared by the parties.³⁰ This rested on an equitable doctrine of common error. As we shall see (10.12), however, the Court of Appeal in '*The Great Peace*' (2002) declared this to be an unsupportable doctrine because it was considered to be inconsistent with a *dictum* of Lord Atkin in the House of Lords in *Bell v. Lever Bros Ltd* (1932).
- (5) *Unilateral error as to substance known to the other party*. The contract is not vitiated if B thinks it is a Picasso and A knows of this error. This is regarded as an 'inoperative' and merely 'unilateral' error as to the contract's 'subject matter'. Such an error does not count.³¹ But this error does operate if B thinks it is a term of the contract that it is a Picasso, provided A knows that B has this special belief.³²

3. SHARED MISTAKE AT COMMON LAW

10.06 Two decisions now dominate this sub-topic. The test for common law mistake, based on the parties' shared erroneous assumption, has been formulated by Lord Atkin in *Bell v. Lever*

25 Under *Derry v. Peek* (1889) 14 App Cas 337, HL (on which see 9.12) and section 2(1) of the 1967 Act (on which see 9.14).

26 Categories known, respectively, as *res sua* (I bought my own thing) or *res extincta* (I bought something which has ceased to exist before the sale, or even which never existed).

27 *Cooper v. Phibbs* (1867) LR 2 HL 149, 170, *per* Lord Westbury; noted by P. Matthews, (1989) 105 LQR 599; on this case, see 10.07.

28 Section 6 of the Sale of Goods Act 1979.

29 *Bell v. Lever Bros Ltd* [1932] AC 161, 224; other restrictive *dicta* in *Leaf v. International Galleries* [1950] 2 KB 86, 89, 94, CA; although *Treitel* (12th edn, London, 2007), 8-020, thinks this too severe.

30 [1950] 1 KB 671, CA.

31 *Smith v. Hughes* (1871) LR 6 QBD 597.

32 On these last two propositions, see *Smith v. Hughes* (1871) LR 6 QBD 597 (common law); *Solle v. Butcher* [1950] 1 KB 671 CA (equitable echo).

Bros Ltd (1932) and by the Court of Appeal in '*The Great Peace*' (2002). Those statements are quoted below, and the cases are considered in turn in the following paragraphs.

In *Bell v. Lever Bros Ltd* (1932) (see 10.07), Lord Atkin said:

[A] mistake will not affect assent unless it is the mistake of both parties, and is as to the existence of some quality which makes the thing without the quality essentially different from the thing as it is believed to be.³³

The Court of Appeal in '*The Great Peace*' (2002) elaborated upon this test and, as we shall see, attempted to render the common law doctrine of shared mistake's core element even more restrictive by formulating a test of strict 'impossibility' (this case is examined at 10.08 and 10.12 ff below). Lord Phillips said:³⁴

[T]he following elements must be present if common mistake is to avoid a contract:

- (i) there must be a common assumption as to the existence of a state of affairs;
- (ii) there must be no warranty by either party that that state of affairs exists;³⁵
- (iii) the non-existence of the state of affairs must not be attributable to the fault of either party;³⁶
- (iv) the non-existence of the state of affairs must render performance of the contract impossible;³⁷
- (v) the state of affairs may be the existence, or a vital attribute, of the consideration to be provided or circumstances which must subsist if performance of the contractual adventure is to be possible.

A rider to (ii), appearing later in the court's judgment, is the proposition that the court must construe the agreement in order to determine whether '[a] party has undertaken the risk that it may not prove possible to perform the contract, and the answer to this question may well be the same as the answer to the question whether the impossibility of performance is attributable to the fault of one or other of the parties'.³⁸

There are numerous cases, mostly decided in the nineteenth century, where supposed transactions were held to be void, that is, rendered a complete nullity, on the basis of common mistake: cases within category A (see the text below) are commonly denoted as instances, or extensions, of *res extincta* (that is, a subject matter which no longer exists); and category B (see the text below) concerns so-called *res sua* (that is, the subject matter

33 [1932] AC 161, 218, HL; generally on this decision, see C. MacMillan, *Mistakes in Contract Law* (Oxford, 2010), 259 ff (for a similarly strict common law decision, cited in the present decision at 207, 218, 233, Blackburn J in *Kennedy v. Panama, New Zealand and Australian Royal Mail Co.* (1867) LR 2 QB 580, 586–8; on which see C. MacMillan, *Mistakes in Contract Law* (Oxford, 2010), 190 ff).

34 [2002] EWCA Civ 1407; [2003] QB 679, at [76].

35 On element (ii) of this test, see *ibid.*, at [75].

36 On element (iii), see *ibid.*, at [77] to [79], noting the High Court of Australia's decision in *McRae v. Commonwealth Disposals Commission* (1951) 84 CLR 377, 408, 410.

37 Cf Lord Radcliffe's radical difference test in *Davis Contractors Ltd v. Fareham Urban District Council* [1956] AC 696, 729, HL, quoted at 16.02.

38 [2002] EWCA Civ 1407; [2003] QB 679 at [84]; on the question whether contract distributes the risk, see *William Sindall plc v. Cambridgeshire County Council* [1994] 1 WLR 1016, 1034H–1035E, CA; see also

of the proposed sale or lease is already owned by the 'purchaser'/'tenant'); many of these decisions are reviewed in the speech of Lord Atkin in *Bell v. Lever Bros Ltd* (1932) and in the judgment of Lord Phillips MR in '*The Great Peace*' (2002) (examined at 10.08 and 10.12 ff below).

The following are examples of *res extincta*:

- (1) A sale of specific goods where the goods have already perished without the seller being aware, as provided by section 6 of the Sale of Goods Act 1979, a provision reflecting the result in *Couturier v. Hastie* (1865).³⁹
- (2) The same would be true of a sale of specific property which has never existed, unless the contract is conceived as wholly aleatory (if so, the buyer would bear the risk of its non-existence) or the seller has impliedly undertaken to bear responsibility if the subject matter does not exist, as in *McRae v. Commonwealth Disposals Commission* (1951).⁴⁰
- (3) A guarantee for the payment of rent on machines (or other property) which does not exist: *Associated Japanese Bank Ltd v. Crédit du Nord SA* (1989).⁴¹
- (4) The sale of an annuity (creating an income stream for a period) on the name of a person who, unknown to the parties to the supposed sale, is already dead: *Strickland v. Turner* (1852).⁴²
- (5) The transfer of a life assurance policy on the life of a person who is, unknown to either party to the transfer, already dead: *Scott v. Coulson* (1903).⁴³
- (6) The renewal of an insurance policy in ignorance of the fact that the assured has already died: *Pritchard v. Merchants' and Tradesman's Mutual Life Assurance Society* (1858).⁴⁴
- (7) The sale of a bill of exchange in fact invalid for forgery (*Gompertz v. Bartlett* (1853))⁴⁵ or invalid for lack of formality (*Gurney v. Womersley* (1854)).⁴⁶

The following is an example of *res sua*:

- (8) The purchase of title or the grant of a lease in a property already owned absolutely by the purchaser or the proposed tenant (on the latter situation, see the facts of *Cooper v. Phibbs* (1867)⁴⁷ at 10.14).

Kalsep Ltd v. X-Flow BV, The Times, 3 May 2001, Pumfrey J, noted by A. Phang, [2002] CLJ 272–3; *Brennan v. Bolt Burdon* [2004] EWCA Civ 1017; [2005] QB 303, at [38] to [40].

39 (1856) 5 HL Cas 673; P. S. Atiyah, (1959) 75 LQR 487; C. MacMillan, *Mistakes in Contract Law* (Oxford, 2010), 181 ff.

40 (1951) 84 CLR 377, High Court of Australia.

41 [1989] 1 WLR 255, Steyn J (where discussion of 'mistake' was technically *obiter*, the case being decided on a question of construction).

42 (1852) 7 Exch 208.

43 [1903] 2 Ch 249, CA.

44 (1858) 3 CB (NS) 622.

45 (1853) 2 E & B 849.

46 (1854) 4 E & B 133.

47 (1867) LR 2 HL 149.

These examples of transactions foundering on the basis of initial and profound miscalculations are easily subsumed within the strict criterion of ‘impossibility’ enunciated in *The Great Peace* (2003): see point (iv) of the extract quoted above from the judgment of Lord Phillips in this case: ‘the non-existence of the state of affairs must render performance of the contract impossible.’

But that criterion cannot prevail and must be reformulated to reflect the earlier case law (including the formulations in *Bell v. Lever Bros Ltd*; see below) and the nuances of commercial disappointment legitimately covered by ‘common mistake’. For example, in ‘the Coronation litigation’ (16.13), a licence to view the procession was held to be void *ab initio*, neither party being yet aware that the Coronation had just been postponed (one hour earlier) because of the King’s ill-health: *Griffith v. Brymer* (1903).⁴⁸ And, in the post-*Great Peace* case law, there are already strong hints that ‘impossibility’ is not the appropriate test. Thus, Sedley LJ in *Brennan v. Bolt Burdon* (2004) attractively suggested that the concept of ‘impossibility’ is too narrow. He suggested that mistake extends to situations where the parties’ shared assumption has proved to be fundamentally unfounded but the contract has not become ‘impossible’.⁴⁹ In *Kyle Bay Ltd v. Underwriters etc.* (2007), Neuberger LJ suggested that the impossibility test and the ‘essential or radical difference’ test are broadly similar.⁵⁰ In *Champion Investments Ltd v. Ahmed* (2004),⁵¹ the judge said that the test was whether the mistake rendered the contract ‘essentially different from what the parties believed it to be’ (*Bell v. Lever Bros Ltd*, on which see 10.07) or ‘did it render performance of the contract impossible’ (*The Great Peace*, on which see the earlier part of this paragraph, and 10.08 and 10.12 ff). It seems clear, therefore, that the ‘essential difference’ test has survived. Furthermore, *Graves v. Graves* (2007) (see 10.11 for details)⁵² shows that impossibility is too stern a test.

10.07 *Bell v. Lever Bros Ltd* (1932).⁵³ The facts were as follows:

Two directors, Bell and Snelling, of a company operating in West Africa, were paid large ‘severance’ payments by a controlling parent company, Lever Brothers Ltd. The latter then discovered that both directors might have been dismissed without compensation because they had committed breaches of their fiduciary⁵⁴ duties towards the African company. Lord Blanesburgh, who was a member of the majority, explained that Lever Brothers had arranged for Bell and Snelling to become directors of the Niger Company and its associated companies,

48 (1903) 19 TLR 434, Wright J.

49 *Brennan v. Bolt Burdon* [2004] EWCA Civ 1017; [2005] QB 303; *Treitel* (12th edn, London, 2007), 8-022 ff; J. Cartwright, *Misrepresentation, Mistake and Non-Disclosure* (2nd edn, 2007), 3.20 ff.

50 [2007] EWCA Civ 57; [2007] Lloyd’s Rep IR 460, at [23] to [25].

51 [2004] EWHC 1956 (QB), at [32], William Blair QC.

52 [2007] EWCA Civ 660; [2008] HLR 10; [2008] L & TR 15; [2007] 3 FCR 26.

53 [1932] AC 161, HL; on the factual background to this case, see C. MacMillan, (2003) 119 LQR 625; C. MacMillan, *Mistakes in Contract Law* (Oxford, 2010), 259 ff; see also A. Chandler, J. Devenney and J. Poole, ‘Common Mistake, Theoretical Justification and Remedial Inflexibility’ [2004] JBL 34–58.

54 *Calvert v. William Hill Credit Ltd* [2008] EWCA Civ 1427; [2009] Ch 330, at [53]; *Parker and Mellows: The Modern Law of Trusts* (9th edn, London, 2008), 10-048 ff; J. Edelman, ‘When Do Fiduciary Duties Arise?’ (2010) 126 LQR 302.

but Lever Brothers were not their employers. Therefore, Lever Brothers did not have the power to 'dismiss' Bell or Snelling from employment.⁵⁵ Lever Brothers sued to recover these sums. To succeed, the claimant company needed to show that the 'golden handshake' agreements were vitiated by a common mistake. But a bare majority of the House of Lords (overturning the decisions of both the lower courts) held that the error was not serious (or 'fundamental') enough.

Lord Atkin, a member of the majority, after noting that a contract can be void if there is an error as to identity (on which see below) or as to the existence of the subject matter at the date of the supposed contract, acknowledged the further possibility of a fundamental error as to the quality of the subject matter. But his test was very narrow:⁵⁶

Mistake as to quality of the thing contracted for raises more difficult questions. In such a case a mistake will not affect assent unless it is the mistake of both parties, and is as to the existence of some quality which makes the thing without the quality essentially different from the thing as it was believed to be.⁵⁷

He gave various examples of errors not satisfying this 'essentially different quality' test:⁵⁸

A buys B's horse; he thinks the horse is sound and he pays the price of a sound horse; he would certainly not have bought the horse if he had known as the fact is that the horse is unsound. If B has made no representation as to soundness and has not contracted that the horse is sound, A is bound and cannot recover back the price. A buys a picture from B; both A and B believe it to be the work of an old master, and a high price is paid. It turns out to be a modern copy. A has no remedy in the absence of representation or warranty. A agrees to take on lease or to buy from B an unfurnished dwelling-house. The house is in fact uninhabitable. A would never have entered into the bargain if he had known the fact. A has no remedy, and the position is the same whether B knew the facts or not, so long as he made no representation or gave no warranty. A buys a roadside garage business from B abutting on a public thoroughfare: unknown to A, but known to B, it has already been decided to construct a bypass road which will divert substantially the whole of the traffic from passing A's garage. Again A has no remedy.

All these cases involve hardship on A and benefit B, as most people would say, unjustly. They can be supported on the ground that it is of paramount importance that contracts should be observed, and that if parties honestly comply with the essentials of the formation of contracts – i.e., agree in the same terms on the same subject matter – they are bound, and must rely on the stipulations of the contract for protection from the effect of facts unknown to them.

In *Bell v. Lever Bros Ltd* (1932), Lord Blanesburgh, another member of the majority, but whose long speech is seldom properly considered, explained the commercial considerations which underpin the majority's decision: first, that the payments under the 'agreements of settlement' were 'sweeteners', intended to secure peace and finality (Lever Brothers entered these agreements to secure the directors' enthusiastic assistance in preparing for the amalgamation of various West African companies; that corporate restructuring would also entail making them redundant); secondly, that the payments were intended to induce them to

⁵⁵ [1932] AC 161, 172, HL.

⁵⁶ *Ibid.*, at 218.

⁵⁷ Compare the more elaborate test in section 6(b) of the New Zealand Contractual Mistakes Act 1977.

⁵⁸ [1932] AC 161, 172, HL, at 218.

resign voluntarily and without controversy; Lever Brothers' interests might have been seriously prejudiced if the directors had proved recalcitrant, and the entire amalgamation had instead misfired.⁵⁹ He explained the matter as follows:⁶⁰

[W]hile undoubtedly the claim for unearned salary amounting at the remote outside in one case to over £17,000 and in the other to £13,000 was a material consideration for the payments agreed to, it was neither on the terms of either letter nor in fact the sole inducing cause. Into that inducement there undoubtedly entered the desire tangibly to recognise the exceptional services rendered to Niger by each appellant acknowledged in each letter and even now affirmed: *still more perhaps to enlist their support of the amalgamation and to have their assistance in carrying it through in all its details to completion: above all, to secure, on May 1 following, the voluntary resignation by each appellant of all his offices, results of value, it may have been of infinite value, to the prospects of a delicate negotiation in the success of which millions of pounds were involved.* And these last two results could not have been secured if Levers, instead of [making the settlement offers], had, with the real offending transactions then disclosed to them, repudiated all further obligations under their agreements with the appellants, and as shareholders in Niger had sought, in spite of the appellants' opposition – quite effective for a sufficiently long period – to remove them from office.⁶¹

In light of these clear statements by Lord Blanesburgh, it is odd that, in the leading historical study of this case, Catherine MacMillan rejects this factor, saying:⁶²

[One suggested] justification [for the majority's decision] is that there were other advantages secured by Lever Brothers, namely the co-operation of Bell and Snelling with the amalgamation. Again, this does not appear from the evidence at trial. In particular, Snelling, away in Africa, was oblivious to the negotiations. In Bell's case, the negotiations were virtually concluded before he was aware that he would not have a role in the new company.

The case was certainly borderline, but it is submitted that Lord Blanesburgh's explanation just about justifies the result. However, some commentators have doubted whether the majority's decision is convincing. For example, the late Professor Sir John Smith contended that the case fell squarely within the scope of a notion of *res sua* or *res extincta* – of the need to imply a 'condition precedent', that is, a tacit term to reflect the obvious fact that the supposed transaction has misfired because a person has bought something he already owns or something which has ceased to exist (this idea of implying conditions precedent or conditions subsequent, rather than employing the technique of 'mistake', remains available as a technique, and as an even more flexible method than mistake: see *Graves v. Graves* at 10.11 below; however, the Court of Appeal in '*The Great Peace*' preferred the method of 'mistake': see 10.08). Smith wrote:⁶³

[W]as not *Bell v. Lever Bros* a case of *res sua*? In substance, Levers were saying to Bell, 'We will pay £30,000 for the right to terminate your employment', a right which

⁵⁹ *Ibid.*, at 200.

⁶⁰ *Ibid.*, at 181, where these factors are encapsulated.

⁶¹ Emphasis added.

⁶² C. MacMillan, (2003) 119 LQR 625, 657; E. McKendrick, *Contract Law: Text, Cases and Materials* (4th edn, Oxford, 2010), 549.

⁶³ (1994) 110 LQR 400, 414–15.

was already theirs. Bell, on the other hand, was saying to Levers, 'I will sell my right to continue in your employment for £30,000'. He had once had such a right, but it no longer existed. It was *res extincta*. Everything depends on how you define the subject matter of the contract. If you say it was the contract of service, then the voidability or otherwise of that contract was a quality; but if you say the subject matter was the right to continue in employment, then the subject matter did not exist. It is thought that the better view is that the substance of the matter was that the subject of the contract was Bell's right to continue in employment.

10.08 '*The Great Peace*' (2002).⁶⁴ In this case, the Court of Appeal applied *Bell v. Lever Bros Ltd* (1932)⁶⁵ to these facts:

In '*The Great Peace*', a salvage company hired the claimant's ship for five days to escort a stricken ship, which was in danger of sinking in the Indian Ocean. A third party source had misled the salvage company into believing that the claimant's ship was closest to the stricken vessel. In fact, another ship was closer to the stricken vessel and so better placed to provide 'stand by' assistance. The Court of Appeal (and, earlier, Toulson J) upheld the claimant's action for the agreed five days' hire. Both courts rejected the salvage company's defence of fundamental mistake. That company had delayed cancelling the hire until it was clear that another ship was closer. This strategic delay showed that, during the period of hesitation, the claimant's ship might have been of use to the salvage company. The Court of Appeal said:⁶⁶ '[T]he fact that the [stricken ship and *The Great Peace*] were considerably further apart than the [defendants] had believed did not mean that the services that *The Great Peace* was in a position to provide were essentially different from those which the parties had envisaged when the contract was concluded.'

It is suggested that this decision is fair and reasonable. The party requiring urgent assistance should surely bear the risk that hastily gathered information might prove to be inaccurate. The terms of the 'rescue' charter did not explicitly transfer this risk of inaccurate information to the claimant rescue-ship owner, for example, by stating that its ship was believed to be 'the closest ship to the casualty'.⁶⁷ And it is arguably in the public interest that contracts for maritime rescue should not be lightly declared void on grounds of mistake.

10.09 *Mistake of law*.⁶⁸ The Court of Appeal in *Brennan v. Bolt Burdon* (2004) has confirmed that a shared mistake concerning a pure point of law can vitiate a contract.⁶⁹ Earlier, the

64 [2002] EWCA Civ 1407; [2003] QB 679; F. M. B. Reynolds, (2003) 119 LQR 177; S. Midwinter, (2003) 119 LQR 180; for other literature considering this decision, see C. MacMillan, in C. Mitchell and P. Mitchell (eds.), *Landmark Cases in the Law of Restitution* (Oxford, 2006), 357 n. 180.

65 [1932] AC 161, HL.

66 [2002] EWCA Civ 1407; [2003] QB 679, at [165].

67 During the parties' discussion, 'closest ship' had been uttered, it seems.

68 On finality and compromises, see N. Andrews, 'Mistaken Settlement of Disputable Claims' [1989] LMCLQ 431.

69 [2004] EWCA Civ 1017; [2005] QB 303; approved in *Meretz Investments NV v. ACP Ltd* [2007] EWCA Civ 1303; [2008] 2 WLR 904, at [118].

fact/law distinction had been discarded by the House of Lords with respect to recovery of mistaken payments in the *Kleinwort Benson* case (1999),⁷⁰ and at first instance for the law of misrepresentation.⁷¹ The Court of Appeal in the *Brennan* case accepted that mistake of law might invalidate a contract of compromise (although not on the present facts: see below). The court held that the compromise in the *Brennan* case was not vitiated. This was because the legal point was doubtful and the 'new law' did not 'come out of the blue'.⁷² And so there was in fact no 'error', merely acquiescence in a doubtful precedent⁷³ soon to be reconsidered by the Court of Appeal.⁷⁴

- 10.10 *Renaissance of the implied term technique.* The Court of Appeal in '*The Great Peace*' (2002) said that 'the theory of the implied term is as unrealistic when considering common mistake as when considering frustration'.⁷⁵ It added: '[A]voidance of a contract on the ground of common mistake results from a rule of law'.⁷⁶ However, the later decision in *Graves v. Graves* (2007) (10.11) shows that the 'implied term technique' has not been jettisoned, although on the facts of that case this technique was used to impose an 'implied condition subsequent' which terminated an agreement.
- 10.11 The 'implied technique' was employed in *Graves v. Graves* (2007).⁷⁷ The Court of Appeal found an 'implied condition subsequent' even though the strict test of initial impossibility was not satisfied.

The facts of the *Graves* case (2007) were as follows. After Mr and Mrs Graves divorced, Mrs Graves received the matrimonial home and maintenance. But she lost the property after failing to pay the mortgage instalments. The former husband allowed her to become a tenant of his property, provided she paid rent. Both parties had assumed that 90 per cent of her rent would be financed by housing benefit. It was later revealed that this was an error (benefit could not be validly paid on these facts; the erroneous assumption made in this case concerned a matter of 'law', but, as the Court of Appeal noted,⁷⁸ such a mistake is now treated as significant). And so the ex-husband applied to evict Mrs Graves. The claim succeeded, but the court found a means of adjusting the parties' relations to achieve broad justice. It held that the tenancy agreement had not been void for mistake. Instead, although initially valid, the agreement had become ineffective by reason of an implied condition subsequent, namely, non-receipt of housing benefit. Without these housing benefit payments, the ex-wife could not pay the rent.

70 *Kleinwort Benson Ltd v. Lincoln City Council* [1999] 2 AC 349, HL.

71 *Pankhania v. Hackney London Borough Council* [2002] EWHC 2441 (Ch); [2002] NPC 123, Deputy Judge Rex Tedd, cited by Kay LJ in the *Brennan* case, [2004] EWCA Civ 1017; [2005] QB 303, at [10].

72 *Brennan* case, [2004] EWCA Civ 1017; [2005] QB 303, at [56].

73 *Ibid.*, at [23].

74 *Anderton v. Clwyd County Council (No. 2)* [2002] 1 WLR 997, CA; N. Andrews, *English Civil Procedure* (Oxford, 2003), 10.18 to 10.19 ('service of documents' under the Civil Procedure Rules 1998).

75 '*The Great Peace*' [2002] EWCA Civ 1407; [2003] QB 679, at [73].

76 *Ibid.*, at [73].

77 [2007] EWCA Civ 660; [2008] HLR 10; [2008] L & TR 15; [2007] 3 FCR 26.

78 *Ibid.*, at [32], citing *Kleinwort Benson Ltd v. Lincoln City Council* [1999] 2 AC 349, HL; and *Brennan v. Bolt Burdon* [2004] EWCA Civ 1017; [2005] QB 303, on which see 10.09.

Upon the contract's cessation (the date of which was the council's notification that the housing benefit rules did not permit the ex-wife to receive payment), the court could adjust the parties' rights (this analysis seems to proceed on general principles of restitution; the court was not exercising an equitable remedy of rescission). In essence (omitting here complications in the calculation of the fair rent for the whole period of the ex-wife's occupancy), the court held that the ex-wife had been liable for a reasonable rent (lower than the level in fact agreed) and that this liability should be set off against the deposit (in respect of rent) which now became repayable by the ex-husband. The ex-wife's liability to pay rent continued until she quit the premises (as she by then had). Her stay had been long enough that she in fact owed the ex-husband nearly £6,400. Thomas LJ held: '[A] condition should be implied into the agreement on the basis of the strict approach to the implication of terms; the term was an implied condition that if housing benefit was not payable, the tenancy would come to an end. Such a condition was, on the evidence, obviously a term of the agreement which Mr and Mrs Graves both plainly intended to form part of their contract.'⁷⁹

4. NO RESCISSION FOR SHARED MISTAKE IN EQUITY: 'THE GREAT PEACE' REPUDIATING SOLLE v. BUTCHER

- 10.12 The Court of Appeal in *'The Great Peace'* (2002) also held that there is no separate equitable doctrine of rescission for shared mistake.⁸⁰ It rejected Denning LJ's decision in *Solle v. Butcher* (1950)⁸¹ which had stood – although admittedly not flourished⁸² – for fifty years. In *Solle v. Butcher*, Denning LJ had said that the equitable remedy of rescission can be awarded in respect of a common or shared mistake concerning a fundamental aspect of the subject matter, provided the party seeking relief was not at fault. Where appropriate, relief would be granted on terms (that is, with strings attached by the court, in order to achieve fairness to both parties).

79 *Graves v. Graves* [2007] EWCA Civ 660; [2008] HLR 10; [2008] L & TR 15; [2007] 3 FCR 26, at [41].

80 [2002] EWCA Civ 1407; [2003] QB 679; K. F. K. Low, 'Coming to Terms with *The Great Peace* in Common Mistake', in J. W. Neyers, R. Bronaugh and S. G. A. Pitel (eds.), *Exploring Contract Law* (Oxford, 2009), 319 ff.

81 *Solle v. Butcher* [1950] 1 KB 671, CA; C. MacMillan, in C. Mitchell and P. Mitchell (eds.), *Landmark Cases in the Law of Restitution* (Oxford, 2006), chapter 12; and she cites (*ibid.*, at 54 n. 166) massive academic literature on the *Solle* case; C. MacMillan, *Mistakes in Contract Law* (Oxford, 2010), 278 ff.

82 Cases applying the *Solle* case had included: *Magee v. Pennine Insurance Ltd* [1969] 2 QB 507, 514–15, CA (Lord Denning MR applying his earlier decision); *West Sussex Properties Ltd v. Chichester District Council* [2000] All ER (D) 887, CA; *Nutt v. Read* (1999) 32 HLR 76, CA; *Laurence v. Lexcourt Holdings Ltd* [1978] 1 WLR 1128; *Grist v. Bailey* [1967] Ch 532 (Hoffmann LJ, in *William Sindall plc v. Cambridgeshire County Council* [1994] 1 WLR 1016, 1035, CA, doubted the validity of both the *Grist* and *Laurence* cases); *Associated Japanese Bank v. Crédit du Nord* [1989] 1 WLR 255, 267–8, Steyn J: '[A] narrow doctrine of common law mistake (as enunciated in *Bell v. Lever Bros Ltd* [1932] AC 161, HL, supplemented by the more flexible doctrine of mistake in equity (as developed in *Solle v. Butcher* [1950] 1 KB 671, CA and later cases), seems to me to be an entirely sensible and satisfactory state of the law.' On this case, see G. H. Treitel, 'Mistake in Contract' (1988) 104 LQR 501; and J. C. Smith, 'Contracts – Mistake, Frustration and Implied Terms' (1994) 110 LQR 400–19; on these decisions, see *'The Great Peace'* [2002] EWCA Civ 1407; [2003] QB 679, CA, at [135] to [151].

10.13 *The three suggested categories of 'equitable mistake' rendering a contract voidable.* In *Solle v. Butcher* (1950), Denning LJ had suggested that there were three categories covered by equitable mistake: (1) misrepresentation (on which see chapter 9); (2) error unconscionably acquiesced in; and (3) shared error.⁸³ These categories will now be elaborated.

- (1) '[A] contract will be set aside if the mistake of one party has been induced by a material misrepresentation by the other, even though it was not fraudulent or fundamental.' This remains good law. This is the topic of rescission for misrepresentation (see chapter 9; and on rescission for fraudulent misrepresentation, by notification to the police, see the discussion of the *Caldwell* case at 10.34 below).
- (2) '[I]f one party, knowing that the other is mistaken about the terms of an offer, or the identity of the person by whom it is made, lets him remain under his delusion and conclude a contract on the mistaken terms instead of pointing out the mistake, which is, I venture to think, the ground on which the defendant in *Smith v. Hughes* would be exempted nowadays.' Lord Phillips MR in '*The Great Peace*' indicated that this aspect of equitable relief was not being swept away:⁸⁴ '[C]ases of fraud and misrepresentation, and undue influence, are all catered for under other existing and uncontentious equitable rules. We are only concerned with the question whether relief might be given for common mistake in circumstances wider than those stipulated in *Bell v. Lever Bros Ltd.*' T. M. Yeo considers a Singaporean decision in which a contract was rescinded in equity because the purchaser had taken advantage of a manifest error in the price at which computers were advertised by the vendor.⁸⁵ As discussed in this book at 3.69, the better view is that there is no need for an equitable doctrine of mistake as to terms, of which the other party is constructively aware. At common law, such a transaction will be void. And (in the absence of a misrepresentation by A), B's error as to subject matter cannot give rise to rescission in equity.⁸⁶
- (3) '[A] contract is also liable in equity to be set aside if the parties were under a common misapprehension either as to facts or as to their relative and respective rights, provided that the misapprehension was fundamental and that the party seeking to set it aside was not himself at fault.' This third category has been declared invalid (see the discussion of '*The Great Peace*' case below).

83 [1950] 1 KB 671, 692–3, CA.

84 '*The Great Peace*' [2002] EWCA Civ 1407; [2003] QB 679, at [156].

85 T. M. Yeo, 'Great Peace: A Distant Disturbance' (2005) 121 LQR 393, noting *Chwee Kin Keong v. Digilandmall.com Pte Ltd* [2005] 1 SLR 502 (Singapore Court of Appeal).

86 *Statoil ASA v. Louis Dreyfus Energy Services LP ('The Harriette N')* [2008] EWHC 2257 (Comm); [2009] 1 All ER (Comm) 1035; [2008] 2 Lloyd's Rep 685, at [98] to [105] (rejecting *Huyton SA v. Distribuidora Internacional de Productos Agrícolas SA de CV* [2003] 2 Lloyd's Rep 780, at [455]); see also *Harrison v. Halliwell Landau* [2004] EWHC 1316 (QB); Andrew Smith J in the *Huyton* case suggested that equity has a wider power to invalidate a contract where B's error (suspected by A) does not concern a *term*, merely the subject matter; but Aikens J's repudiation of this liberal approach is persuasive).

Denning LJ in *Solle v. Butcher* (1950) had adopted as support for category (3) above the House of Lords decision in *Cooper v. Phibbs* (1867).⁸⁷

In *Cooper v. Phibbs* (1867), an uncle had spent money improving an Irish salmon fishery. He then leased it to his nephew. The parties were mistaken as to their legal position. In fact, the nephew was already the owner of it (as tenant for life).⁸⁸ The parties were acting, therefore, under a mistake as to their private rights. The nephew's application for rescission was upheld (this was an application to a court of equity for the setting aside of the contract and consequential relief). But the House of Lords added the condition that allowance should be made in the uncle's favour for the improvements he had made to the fishery. This was worked out by the imposition of a lien in the uncle's favour. Because the uncle had died, the benefit of the lien accrued in favour of the trustee for the uncle's daughters. The basis of this decision has been disputed. Chitty⁸⁹ cites this 1867 case as a possible example of equity applying 'general principles of restitution' in the context of a void transaction, but Paul Matthews has contended that the case, properly scrutinised, did not concern a contract void at common law.⁹⁰ Instead, it does appear that the contract was regarded by the House of Lords as subsisting until set aside.

Whichever view is taken of *Cooper v. Phibbs* (1867), Catherine MacMillan contends that 'prior to *Cooper v. Phibbs* there *was a* remedy given by Courts of Equity to rescind a contract for mistake'.⁹¹ So Denning LJ in the *Solle* case was not creating a new jurisdiction in equity. And it is unfortunate that there was no final appeal to the House of Lords in the *Solle* case, leave for such an appeal had been given, but the parties then decided not to pursue a further appeal.⁹²

But, even if Denning LJ had been correct in the *Solle* case to regard *Cooper v. Phibbs* (1867) as authority for this equitable doctrine concerning fundamental shared mistake, this is not the end of the story. For, as the Court of Appeal in '*The Great Peace*' (2002) noted, the *Cooper* case (1867) had been reclassified by Lord Atkin in the House of Lords in a *dictum* in *Bell v. Lever Bros Ltd* (1932) as an instance of common law mistake, that is, of a *void* rather than a voidable contract.⁹³ The Court of Appeal in '*The Great Peace*' boldly declared that Lord Atkin's passing remark in *Bell v. Lever Bros Ltd* justified, indeed required, abandoning subsequent Court of Appeal decisions in which the courts had applied the doctrine of *Solle v. Butcher* (1950), or assumed its validity.⁹⁴ The Court

87 (1867) LR 2 HL 149, 170, *per* Lord Westbury; P. Matthews, (1989) 105 LQR 599; C. MacMillan, *Mistakes in Contract Law* (Oxford, 2010), 62 ff.

88 P. Matthews, (1989) 105 LQR 599, at 606, shows that he was owner under an equitable title.

89 Chitty on Contracts (30th edn, London, 2008), 5-062.

90 (1989) 105 LQR 599.

91 C. MacMillan, in C. Mitchell and P. Mitchell (eds.), *Landmark Cases in the Law of Restitution* (Oxford, 2006), at 355 n. 172.

92 *Ibid.*, noting 66 TLR (Pt 1) 448, 468.

93 '*The Great Peace*' case, [2002] EWCA Civ 1407; [2003] QB 679, at [113] to [118], and [126] to [130], especially noting the analysis of Lords Blanesburgh and Atkin, respectively, in *Bell v. Lever Bros Ltd* [1932] AC 161, 190, 218, HL.

94 On these later authorities, see '*The Great Peace*' case, [2002] EWCA Civ 1407; [2003] QB 679, at [135] to [152].

of Appeal in *'The Great Peace'* concluded: '[W]e can see no way that *Solle v. Butcher* can stand with *Bell v. Lever Bros.*'⁹⁵

It must be said that Lord Atkin's passing remark in *Bell v. Lever Bros Ltd* is a fragile basis on which to conclude that the House of Lords in that 1932 decision had jettisoned the equitable doctrine of rescission for shared mistake. Indeed, before 1966, the House of Lords had been bound by its earlier decisions.⁹⁶ Even a *dictum* by Lord Atkin could not annihilate the House of Lords' statement in *Cooper v. Phibbs* (1867) that there is an equitable doctrine to relieve parties from a contract vitiated for shared fundamental error.

- 10.14 How might *'The Great Peace'* (2002) have been assessed on final appeal to the Supreme Court? Denning LJ's suggested equitable doctrine of shared mistake offered three advantages when compared with the common law doctrine of shared mistake concerning the supposed agreement's terms or substance. The first alleged advantage would be that equity might be deployed to widen the ambit of operative shared mistake beyond the narrow limits recognised at common law. The objection to this, however, is that the stability of contracts might be seriously threatened by a broader approach to 'shared mistake'. The second alleged advantage is that the equitable technique of rescission can protect the interests of innocent third parties. This is because the contract is merely voidable, and so it subsists until rescinded. Rescission would be 'barred' if a third party, dealing in good faith, without notice and for value, had bought or acquired rights in the subject matter of the purported agreement. The final alleged advantage is that rescission can be ordered 'on terms'.⁹⁷ The effect can be to keep the contract alive. But this is controversial because this effectively re-makes the bargain for the parties. How should one assess these points? The first alleged advantage is no advantage at all. The second and third alleged advantages are respectable arguments, but they lack sufficient weight to justify a Supreme Court decision to reinstate the *Cooper v. Phibbs* and *Solle v. Butcher* line of authority.⁹⁸

However, in Canada, the Ontario Court of Appeal in *Miller Paving Ltd v. B Gottardo Construction Ltd* (2007) expressed its wish to preserve the equitable doctrine of shared mistake.⁹⁹ Rejecting *'The Great Peace'*, Goudge JA said: 'The loss of the flexibility needed to correct unjust results in widely diverse circumstances that would come from eliminating the equitable doctrine of common mistake would, I think, be a step backward.'

⁹⁵ *Ibid.*, at [160].

⁹⁶ A practice note relaxed until the House of Lords' Practice Statement [1966] 3 All ER 77, enabling that court, in exceptional situations, to reverse one of its decisions.

⁹⁷ E.g. complicated terms imposed by Stirling J, setting aside an agreement based on common mistake, *Allcard v. Skinner* [1896] 2 Ch 369, 384–5; for more recent cases, see *'The Great Peace'* [2002] EWCA Civ 1407; [2003] QB 679, at [103] to [106].

⁹⁸ In New Zealand, the court has received considerable 'remedial flexibility' when deciding whether to uphold or set aside a contract vitiated by mistake: Contractual Mistakes Act 1977, section 7.

⁹⁹ [2007] ONCA 422; (2007) 86 OR (3d) 161; (2007), 285 DLR (4th) 568, at [26], Ontario Court of Appeal; and considering J. McCamus, 'Mistaken Assumptions in Equity: Sound Doctrine or Chimera?' (2004) 40 *Canadian Business Law Journal* 46–86; for references to other common law jurisdictions on this topic, see A. Phang, 'Doctrine and Fairness in the Law of Contract' (2009) 29 LS 534, 542 ff.

- 10.15 *Mistake: comparison with the 'soft law' codes.* In English law, the (not entirely uncontroversial) rejection in *'The Great Peace'* (10.08, 10.12 ff) of a doctrine of equitable shared mistake concerning the nature of the subject matter has left isolated the common law concept of shared mistake rendering the supposed transaction void (10.06 to 10.08). English adoption at common law of the concept of voidness can be contrasted with the (non-binding) schemes of both PECL, *Principles of European Contract Law*, and UNIDROIT's *Principles of International Commercial Contracts* (2004), where 'initial impossibility' is expressly stated not to be a ground of invalidity (PECL, Article 4:102; UNIDROIT,¹⁰⁰ Article 3.3; contrast on this point English law, where the contract will be void: see 10.06 ff), and shared serious error can only render the contract voidable: (PECL, Articles 4:103, 4:112 to 4:116; UNIDROIT,¹⁰¹ Articles 3.4, 3.5, 3.12 to 3.18).

5. UNILATERAL ERROR CONCERNING SUBJECT MATTER

- 10.16 There is no ground for relief at common law if A suffers a mere mistake as 'to the substance' of the subject matter, even if this is known to B. Hence, there is the paradox that it is in A's interest to show that B innocently shared A's error (the situation then becomes one of shared mistake).¹⁰²
- 10.17 *Smith v. Hughes* (1871) established that A's error must not only be known to B, but the error must relate to the supposed *terms of the contract*¹⁰³ (for an example of this, see *Hartog v. Colin & Shields* (1939),¹⁰⁴ where the buyer took advantage of the seller's obvious error concerning the price of hare skins; and see also the discussion of this topic at 3.63 ff, including (at 3.65) Aikens J in the *Statoil* case (2008)).¹⁰⁵

Knowledge extends to imputed knowledge. In *OT Africa v. Vickers plc* (1996), Mance J said:¹⁰⁶

The question is what is capable of displacing that objective agreement. The answer on the authorities is a mistake by one party of which the other knew or ought reasonably to have known. I accept that this is capable of including circumstances

100 2nd edn, Rome, 2004; see M. J. Bonell (ed.), *The UNIDROIT Principles in Practice: Case Law and Bibliography on the UNIDROIT Principles of International Commercial Contracts* (2nd edn, Ardsley, NY, 2006), 191 ff; S. Vogenauer and J. Kleinheisterkamp (eds.), *Commentary on the UNIDROIT Principles of International Commercial Contracts* (Oxford, 2009), 408 ff.

101 2nd edn, Rome, 2004; see M. J. Bonell (ed.), *The UNIDROIT Principles in Practice: Case Law and Bibliography on the UNIDROIT Principles of International Commercial Contracts* (2nd edn, Ardsley, NY, 2006), 193 ff; S. Vogenauer and J. Kleinheisterkamp (eds.), *Commentary on the UNIDROIT Principles of International Commercial Contracts* (Oxford, 2009), 411 ff.

102 A. Tettenborn, *An Introduction to the Law of Obligations* (London, 1984), 169.

103 (1871) LR 6 QB 597; J. Phillips, in C. Mitchell and P. Mitchell (eds.), *Landmark Cases in the Law of Contract* (Oxford, 2008), 205 ff.

104 [1939] 3 All ER 566, Singleton J.

105 *Statoil ASA v. Louis Dreyfus Energy Services LP ('The Harriette N')* [2008] EWHC 2257 (Comm); [2009] 1 All ER (Comm) 1035; [2008] 2 Lloyd's Rep 685, at [95]; J. Cartwright, 'Unilateral Mistake in the English Courts: Reasserting the Traditional Approach' (2009) *Singapore Journal of Legal Studies* 226–34.

106 [1996] 1 Lloyd's Rep 700, 703, Mance J ('knowledge' to include imputed knowledge): see 10.17, 3.65.

in which a person refrains from or simply fails to make enquiries for which the situation reasonably calls and which would have led to discovery of the mistake. But there would have, at least, to be some real reason to suppose the existence of a mistake before it could be incumbent on one party or solicitor in the course of negotiations to question whether another party or solicitor meant what he or she said.

This was considered in *Champion Investments Ltd v. Ahmed* (2004).¹⁰⁷

The restrictive approach adopted in *Smith v. Hughes* (1871) was restated by Lord Atkin in *Bell v. Lever Bros Ltd* (1932).¹⁰⁸ Furthermore, as Denning LJ noted in *Solle v. Butcher*, equity mirrors this common law restriction.¹⁰⁹ In *BCCI v. Ali* (2002), Lord Hoffmann took the opportunity to reaffirm the general merits of the *Smith v. Hughes* doctrine:¹¹⁰ '[T]here is obviously room in the dealings of the market for legitimately taking advantage of the known ignorance of the other party.'¹¹¹ This is a wise comment. A negotiating party's decision to take advantage of the other's commercial misperception of the subject matter's value or quality should not be outlawed: this is part of the rough-and-tumble of many negotiations (compare the *recommendation*, however, of Berg in the context of express negotiation obligations; criticised in this text at 2.09 and 21.12). Morality and law cannot be perfectly congruent. The Court of Appeal in *BCCI v. Ali* (2000) had suggested (see 3.69 for the details) that *Smith v. Hughes* might not reflect modern perceptions of fairness;¹¹² but this case was decided by the House of Lords on a different basis (construction of a written contract of release or compromise).¹¹³

6. DENIAL OF SPECIFIC PERFORMANCE

10.18 Unlike the doctrine of mistake as to terms discussed at 10.17, equity will refuse specific performance even if the error relates merely to the nature of the subject matter of the contract, as opposed to the price or terms regarding that property (specific performance is an *exceptional* equitable remedy; it is normally confined to agreements for the transfer of interests in land or shares in private companies: see 18.14 ff). But equity will refuse this remedy only if the defendant's error was either induced¹¹⁴ by the claimant, or the claimant was aware of the other's error and unconscionably failed to disabuse him (specific performance will also be withheld when the relevant contract is

107 [2004] EWHC 1956 (QB), at [34] and [35], William Blair QC.

108 [1932] AC 161, 224, *per* Lord Atkin.

109 *Solle v. Butcher* [1950] 1 KB 671, 692 (bottom of page), CA.

110 *BCCI v. Ali* [2002] 1 AC 251, HL, at [70].

111 But, here, Lord Hoffmann said the bank had no knowledge of the claim in question: *ibid.*, at [72].

112 [2000] 3 All ER 51, CA.

113 *BCCI v. Ali* [2002] 1 AC 251, HL, at [10], [17], [19], [35] and [86]; *Brennan v. Bolt Burdon* [2004] EWCA Civ 1017; [2005] QB 303.

114 Cf *Denny v. Hancock* (1870) 6 Ch App 1 (buyer's error induced partly by vendor's ambiguous plans; specific performance refused).

voidable by reason of misrepresentation,¹¹⁵ undue influence, duress or unconscionable conduct).¹¹⁶

- 10.19 This restrictive approach to unilateral error in this context derives from *Tamplin v. James* (1880).¹¹⁷ The defendant, a purchaser of real property, could not escape the award against him of specific performance merely because he had misunderstood the precise boundary and scope of an inn when deciding to buy it at auction. This was an instance of *spontaneous* and unilateral error: an error neither *induced* by anything said by the claimant, nor *known* to the claimant. The Court of Appeal in the *Tamplin* case refused to follow earlier decisions, notably, *Malins v. Freeman* (1837),¹¹⁸ in which the claimant's inducement or bad faith knowledge had not been required. The explanation for this change of approach in the *Tamplin* case is that, by 1880, the objective principle in contract law (3.57 ff) had become entrenched. That principle prevents the courts from exonerating a party from obligations under an apparent contract merely because, as a result of his unilateral error, he has entered a disadvantageous contract.¹¹⁹

7. 'NON EST FACTUM': FUNDAMENTAL ERROR IN SIGNED DOCUMENTS¹²⁰

- 10.20 *Non est factum* is a very old common law doctrine. It generously protects someone who signs a deed or other written agreement, for the doctrine is capable of rendering that apparent agreement void (rather than merely voidable). The test is whether the document's contents are wholly or radically different from those which the signatory assumed them to be. Normally, this doctrine arises if someone, usually the other party, tricks a person into signing the document. But the doctrine can also operate without the mistaken party having to show that the other party induced this error or was aware of it. It follows that the doctrine is an exception to the objective test of agreement (on that topic, see 3.57). In the absence of deception by the other party or a third party, the

115 G. H. Jones and W. Goodhart, *Specific Performance* (2nd edn, London, 1998), 86 ff, also discussing refusal of specific performance on the ground of non-disclosure.

116 *Ibid.*, at 112–16; e.g. *Walters v. Morgan* (1861) 3 De G F & J 718 (defendant hurried by claimant into signing contract without knowing property's true value); *Webster v. Cecil* (1861) 30 Beav 62 (claimant's offer of £2,000 refused; defendant, by error, offering property for £1,250 rather than £2,250); cf the snapping-up case at common law, *Hartog v. Colin & Shields* [1939] 3 All ER 566; cf *Centrovincial Estates plc v. Merchant Investors Assurance Co. Ltd* [1983] Com LR 158, CA (on the last two decisions see 3.63 and 3.65).

117 (1880) 15 Ch D 215, CA; G. H. Jones and W. Goodhart, *Specific Performance* (2nd edn, London, 1998), 12–13, 104 ff.

118 (1837) 2 Keen 25; *Meagher, Gummow and Lehane's Equity: Doctrines and Remedies* (4th edn, Sydney, 2003), 20–090.

119 G. H. Jones and W. Goodhart, *Specific Performance* (2nd edn, London, 1998), 106–7; D. Friedmann, (2003) 119 LQR 68.

120 *Gallie v. Lee* [1971] AC 1004, HL; *United Dominions Trust Ltd v. Western* [1976] QB 513, CA; see also: *Lloyds Bank plc v. Waterhouse, The Independent*, 27 February 1990, CA (J. Cartwright, [1990] LMCLQ 338); *Norwich & Peterborough Building Society v. Steed* (No. 2) [1993] Ch 116, CA; *Schwartz v. Barclays Bank plc* [1995] TLR 452, CA.

doctrine will normally require the signatory to lack real understanding of the document by reason of defective education, illness or innate incapacity. If the signatory is a healthy and not disadvantaged person of ordinary capacity, it would be remarkable, and arguably unprincipled, to declare void a signed contract or deed simply on the basis that the signatory made a fundamental error in his reading of a document (assuming, of course, that the error was neither induced by the other party nor by a third party).

- 10.21 It is questionable whether the *non est factum* doctrine should be retained. Certainly, its extension to non-fraudulently induced mistake is unattractive. For this reason, modern decisions have restricted its scope in three main ways: first, there must be a radical or substantial difference between the document signed and that to which the signatory believed himself to be assenting;¹²¹ secondly, his decision not to read a document will nearly always exclude this doctrine¹²² (in Australia,¹²³ it has been held that the signatory's carelessness precludes resort to *non est factum* only if that plea might affect a third party: for the position in England, see the remainder of this paragraph); thirdly, as *Chitty* notes, by reference to *Lloyds Bank v. Waterhouse* (1990),¹²⁴ the 'ordinary principles' of misrepresentation will apply where A signs as a result of B's misrepresentation (rather than because of a third party's misrepresentation) and the validity of the A/B transaction does not affect a third party.

8. DEEDS AND 'VOLUNTARY INSTRUMENTS' VOIDABLE IN EQUITY

- 10.22 Taken together, Millett J's decision in *Gibbon v. Mitchell* (1990)¹²⁵ and Lewison J's in *Re Griffiths* (2008)¹²⁶ establish the following three points. First, equity can set aside a deed, or other unilateral instrument, which was intended to achieve a specific purpose but, through a mistake on the part of the professional advisors who drew up the deed, the instrument either did not achieve that purpose at all or it achieved something in addition.¹²⁷ Secondly, as made clear by Lewison J in *Re Griffiths* (2008), the jurisdiction is not restricted to errors concerning the effect of a disposition but can include an error about an existing fact if, in the absence of this error, the relevant instrument would not have been executed.¹²⁸ It is enough that the error was 'sufficiently serious' in this sense¹²⁹ (citing a neglected House of Lords authority, *Ogilvie v. Allen* (1899),¹³⁰

121 *Gallie v. Lee* [1971] AC 1004, HL.

122 *United Dominions Trust Ltd v. Western* [1976] QB 513, CA; *Hambros Bank Ltd v. British Historic Buildings Trust* [1995] NPC 179.

123 *Petelin v. Cullen* (1975) 132 CLR 355, High Court of Australia.

124 *Lloyds Bank plc v. Waterhouse, The Independent*, 27 February 1990, CA (J. Cartwright, [1990] LMCLQ 338), noted by *Chitty on Contracts* (30th edn, London, 2008), 5–102.

125 [1990] 1 WLR 1304.

126 [2008] EWHC 118 (Ch); [2009] 2 WLR 394.

127 *Gibbon v. Mitchell* [1990] 1 WLR 1304, 1308H, *per* Millett J.

128 [2008] EWHC 118 (Ch); [2009] 2 WLR 394.

129 *Ibid.*, at [25] and [27].

130 (1899) 15 TLR 294, 295, HL (cited in *Re Griffiths* [2008] EWHC 118 (Ch); [2009] 2 WLR 394, at [20]).

which was expressed in wide terms). It is unnecessary to show precisely what alternative arrangement (if any) would have been made if the error had not affected the disponent's mind.¹³¹ Thirdly, all such errors render the relevant instrument voidable, rather than void.¹³²

9. MISTAKE CONCERNING A PARTY'S IDENTITY¹³³

10.23 *The standard problem.* The source of this vexatious 'mistake' problem is that a rogue, X, pretending to be Y, dupes C into selling goods to X, and X then sells the same goods to D, the sub-purchaser, who buys them in good faith. X absconds and falls out of the picture. The law has a choice between two analyses: that D has acquired good title from X (the latter having received a voidable title when he dealt with C); or that C remains owner because X had derived no title from C which he might transfer to D (under the principle of *nemo dat quod non habet*, D is unprotected if X lacked even a voidable title). As we shall see, in the 'face-to-face' context, *Lewis v. Averay* (1972)¹³⁴ (10.36) shows that the law inclines strongly (although, even now, perhaps not invariably) towards the former analysis, that the transaction is merely voidable; and this will protect the innocent sub-purchaser if the head vendor fails to rescind the main transaction before the moment when the sub-purchase took place; whereas, in the other context, when the dealings between C and X do not involve face-to-face contact, the competing analysis persists and the transaction between C and X is void rather than merely voidable: *Cundy v. Lindsay* (1878)¹³⁵ (10.25).

10.24 The leading decision on error as to identity is *Shogun Finance Ltd v. Hudson* (2004)¹³⁶ (10.29 to 10.32). It contains suggestions that the pre-existing case law is in 'disarray'¹³⁷ and even a 'quagmire'.¹³⁸ However, there is now a causeway over this quagmire, for the *Shogun* case reviews the whole topic, and preserves the important precedents in *Cundy v. Lindsay* (1878)¹³⁹ (10.25) and *Lewis v. Averay* (1972)¹⁴⁰ (10.36).

10.25 *Distance dealings: voidness at common law.* In *Cundy v. Lindsay* (1878),¹⁴¹ Lindsay, a firm of Belfast linen suppliers, was duped by Blenkarn into sending handkerchiefs to him on

131 [2008] EWHC 118 (Ch); [2009] 2 WLR 394, at [27].

132 *Ibid.*, at [31] to [35].

133 D. W. McLaughlan, 'Parol Evidence and Contract Formation' (2005) 121 LQR 9; C. MacMillan, 'Mistake as to Identity Clarified?' (2004) 120 LQR 368; A. Phang, P.-W. Lee and P. Koh, 'Mistaken Identity in the House of Lords' [2004] CLJ 24; R. Stevens, 'Objectivity, Mistake and the Parol Evidence Rule', in A. Burrows and E. Peel (eds.), *Contract Terms* (Oxford, 2007), chapter 6, at 110 ff; Law Reform Committee, *Transfer of Title to Chattels* (Twelfth Report of the Law Reform Committee, Cmnd 2958, 1966).

134 [1972] 1 QB 198, CA.

135 (1878) 3 App Cas 454, HL.

136 [2003] UKHL 62; [2004] 1 AC 919, HL.

137 *Ibid.*, at [5], *per* Lord Millett.

138 *Ibid.*, at [4], *per* Lord Millett.

139 (1878) 3 App Cas 454, HL.

140 [1972] 1 QB 198, CA.

141 (1878) 3 App Cas 454, HL; C. MacMillan, *Mistakes in Contract Law* (Oxford, 2010), 230 ff.

credit. The transaction was for a purchase by 'Blenkiron & Co.', a reputable firm known to Lindsay. Accordingly, Lindsay sent the goods to 'Messrs Blenkarn & Co.'. But, having fallen prey to Blenkarn's fraud, Lindsay was misled into sending these goods to the wrong address, where Blenkarn was able to misappropriate them (Blenkiron & Co.'s premises were at 123 Wood Street, Cheapside, London, but Blenkarn had requested delivery to 37 Wood Street, where he had deviously taken temporary accommodation, in order to take delivery of the fruits of his fraud). Blenkarn, the 'rogue', then sold the goods to Cundy, who bought in good faith.

There were two possible ways of considering the dealings between Blenkarn and Lindsay. First, these dealings might have been considered as an acceptance by Lindsay, the supplier of the goods, of an offer to buy emanating from *the occupier of 37 Wood Street without reference to his name* (if so, a contract between Lindsay and Blenkarn might arise, and it would be voidable because of the latter's fraud). Or this situation could be treated as Lindsay's acceptance of an offer emanating from Blenkiron & Co. (if so, there would be no contract, because there was in fact no true offer made by Blenkiron & Co.; and so, in the absence of any contract between Lindsay and Blenkiron & Co., interception by the rogue Blenkarn would not give him even a voidable title).

10.26 At first instance, the first interpretation was adopted. The court emphasised that the goods had been sent to the rogue's address.¹⁴² However, the Court of Appeal and House of Lords reversed this. They held that the true supposition was that Lindsay was dealing with 'Blenkiron & Co.', but there was no substance at all to these dealings, Blenkiron not having made any offer to Lindsay. Instead, the purported transaction between Lindsay and Blenkarn was void. It was further held that no property passed to the rogue under that contract. Hence, no property could be passed to the defendant, Cundy, the sub-purchaser.¹⁴³ And so Cundy was found liable for the tort of conversion and ordered to pay damages representing the value of the goods. This is a strict tort, which does not require the defendant to have been aware that the goods remained the claimant's property.

10.27 In the House of Lords, Lord Cairns LC emphasised that Lindsay had never heard of Blenkarn and had not the slightest intention of dealing with him: 'Their minds

¹⁴² *Lindsay v. Cundy* (1876) 1 QBD 348 (Blackburn, Mellor and Lush JJ: valid contract between claimant and the commercial entity at 37 Wood Street; decision preferred, audaciously, by Denning LJ in *Solle v. Butcher* [1950] 1 KB 671, 693, CA); for decisions (also examined in the *Cundy* case) concerning goods clearly delivered to A but intercepted or misappropriated by a fraudulent rogue, see *Hardman v. Booth* (1863) 1 H & C 803 (noted in *Shogun* [2003] UKHL 62; [2004] 1 AC 919, HL, at [89], [91], [129] to [130] and [186]); *Hollins v. Fowler* (1874–5) LR 7 HL 757; on *Boulton v. Jones* (1857) 2 H & N 564, Court of Exchequer, see Lord Millett in *Shogun* [2003] UKHL 62; [2004] 1 AC 919, HL, at [94] to [97], and Lord Phillips at [126] (on *Hardman v. Booth*, C. MacMillan, *Mistakes in Contract Law* (Oxford, 2010), 224 ff).

¹⁴³ W. Swadling, 'Rescission, Property, and the Common Law' (2005) 121 LQR 123 (controversially contending that title should not be re-vested in the vendor until rescission, and that vendor's error as to the (fraudulent) buyer's creditworthiness should result in personal – but not proprietary – protection of vendor).

never, even for an instant of time rested upon him, and as between him and them there was no consensus of mind which could lead to any agreement or any contract whatever.¹⁴⁴ This was treated as a clear situation where A intended to contract with B, a real entity, and not with X. This was not a mistake as to X's creditworthiness, but an error concerning X's true identity. None of the dealings involved face-to-face contact between A and X. The decision is generous to the claimant, who might have taken greater care to check that Blenkinson & Co. really did do business at 37 Wood Street.

- 10.28 *Cundy v. Lindsay distinguished*. The Court of Appeal in *King's Norton Metal Co. v. Edridge Merritt & Co. Ltd* (1897) distinguished *Cundy v. Lindsay*.¹⁴⁵ C delivered on credit a ton of brass rivet wire to X. X was masquerading as a company of substance, 'Hallam & Co.'. But there was no such company. X sold the goods to D. The Court of Appeal held that there was a contract between C and X, namely, a contract with 'the writer of the letters'. *Cundy v. Lindsay* was distinguished because in that earlier case the vendor had intended to deal with Blenkinson & Co., a real entity known to that party.¹⁴⁶ *Cundy v. Lindsay* was also distinguished nearly a hundred years later by Waller J in *Citibank NA v. Brown Shipley* (1991).¹⁴⁷ But a majority of the House of Lords in *Shogun Finance Ltd v. Hudson* (2004) narrowly endorsed the view, supported by *Cundy v. Lindsay*, that a supposed contract can be void for error as to identity.¹⁴⁸

- 10.29 *The Shogun case: upholding Cundy v. Lindsay*. In *Shogun Finance Ltd v. Hudson* (2004), X impersonated Patel to acquire a Mitsubishi Shogun car under a credit arrangement. The garage-owner, Varieva, sold the car to C, a hire-purchase credit company. X had tricked both C (with which all dealings were by fax or telephone) and Varieva into believing that X was Patel (the latter being a real person). X used Patel's stolen driving licence to bolster the fraud. C checked Patel's credit rating before agreeing to proceed. A written hire-purchase agreement was then concluded in writing between C and Patel. Although X paid part of the deposit of 10 per cent in cash, he gave a bad cheque for the remainder of the deposit.¹⁴⁹ After driving the car away, X soon sold it to D, who bought it in good faith. X then disappeared without trace. The hire-purchase legislation creates an exception to the *nemo dat quod non habet* principle in this hire-purchase context if the ultimate purchaser, D, has bought in good faith from 'the debtor'. Section 27(2) of the Act provides:¹⁵⁰

144 (1878) 3 App Cas 459, 464–5, HL; also Lord Hatherley at 469 and Lord Penzance at 471.

145 (1897) 14 TLR 98, CA; explained in the *Shogun* case, [2003] UKHL 62; [2004] 1 AC 919, HL, at [3], [77], [78], [134] and [135].

146 (1897) 14 TLR 98, 99, CA.

147 [1991] 2 All ER 690.

148 [2003] UKHL 62; [2004] 1 AC 919, HL.

149 The cheque was probably made in Patel's name: *ibid.*, at [115], Lord Phillips.

150 Section 27(2) of the Hire Purchase Act 1964 (as substituted by section 192(3)(a) of and Schedule 4, para. 22, to the Consumer Credit Act 1974).

Where the disposition ... is to a private purchaser, and he is a purchaser of the motor vehicle in good faith without notice of the hire-purchase ... agreement ... that disposition shall have effect as if the creditor's title to the vehicle has been vested in the debtor immediately before that disposition.

The question was whether the word 'debtor' referred to Patel or to X on the present facts. In other words, was there a hire-purchase agreement between C and X, or between C and Patel, as the document itself declared? If the latter, no obligations would arise between C and Patel. This was because Patel's signature had been forged and he had known nothing of these events.¹⁵¹

10.30 *Majority in the Shogun case.* A bare majority (Lords Hobhouse, Phillips and Walker; Lords Nicholls and Millett dissenting) held that the statutory word 'debtor' (see 10.29) denoted the person named in the document itself, namely, Patel. They held that the dealings for the hire-purchase contract had not taken place face-to-face but by fax and telephone, involving communications from the car dealer's showroom to the credit company's offices.¹⁵² They affirmed that the identity of parties to a written agreement is established by the names stated in that agreement¹⁵³ (however, D. W. McLaughlan contends that the parol evidence rule should not be conclusive and that extrinsic evidence should be admissible to determine whether there was consensus or instead a fundamental error as to identity).¹⁵⁴ Indeed, Lord Hobhouse (a member of the majority) considered the written identification of 'Patel' as conclusive, and so he was wholly unimpressed by counsel's discussion in this litigation of 'mistake as to person'.¹⁵⁵ Three things followed from the majority decision: first, no hire-purchase agreement had been entered between C and X; secondly, therefore, in his dealings with X, D was unprotected by the hire-purchase exception to the *nemo dat quod non habet* principle; finally, C had a good claim for conversion against D (as had been held at first instance and by a majority of the Court of Appeal).¹⁵⁶

10.31 *Dissenting speeches in the Shogun case:* Lords Nicholls and Millett said that C had intended to deal with X, the rogue in the showroom, and not with Patel. C had believed X and Patel to be the same person.¹⁵⁷ They proposed that the courts should use the 'voidable' title analysis (already used in face-to-face contexts: see 10.36 below) in this 'distance dealing'

151 *Shogun* [2003] UKHL 62; [2004] 1 AC 919, HL at [56] *per* Lord Millett, and [178] *per* Lord Phillips.

152 *Ibid.*, at [51], *per* Lord Hobhouse; *ibid.*, at [167], [176] and [179], *per* Lord Phillips; and *ibid.*, at [191], *per* Lord Walker.

153 Upholding *Dyson and Brooke LJ* in the Court of Appeal below; and applying *Hector v. Lyons* (1989) 58 P & CR 156, CA, at 158–9, 160.

154 D. W. McLaughlan, 'Parol Evidence and Contract Formation' (2005) 121 LQR 9.

155 *Shogun* [2003] UKHL 62; [2004] 1 AC 919, HL, at [52] to [55], and [45] to [49].

156 *Ibid.*, at [52], *per* Lord Hobhouse: although not pleaded in this case, the garage-owner had also committed conversion by placing the car into the hands of X after the credit company, C, had received title.

157 *Ibid.*, at [38] to [41], *per* Lord Nicholls; and *ibid.*, at [105] to [107], *per* Lord Millett.

situation. Accordingly, they suggested that the House should overrule *Cundy v. Lindsay* (1878).¹⁵⁸ Lord Millett attacked the supposed critical distinction between face-to-face and 'distance dealings'.¹⁵⁹ He formulated this principle thus:

While a person cannot intercept and accept an offer made to some one else, he should normally be treated as intending to contract with the person with whom he is dealing. Provided that the offer is made to him, then whether his acceptance of the offer is obtained by deception or mistake, and whether his mistake is as to the identity of the offer or some material attribute of his, the transaction should result in a contract, albeit one which is voidable.¹⁶⁰

Lord Millett also suggested that the sub-purchaser's interests should be preferred rather than the swindled seller 'who had an opportunity to uncover the fraud'.¹⁶¹ Lord Nicholls agreed.¹⁶² However, Lord Walker (one of the majority) challenged the dissenters' preference for the sub-purchaser rather than the swindled vendor: '[I]t would not be right to make any general assumption as to one innocent party being more deserving than the other'.¹⁶³ The dissenters' approach had been supported earlier by Denning LJ's opinion in *Solle v. Butcher* (1950)¹⁶⁴ and by the Law Reform Committee (1966).¹⁶⁵

10.32 *Assessment of the Shogun case.* It is submitted that the majority's decision itself in *Shogun Finance Ltd v. Hudson* (2004) is sound because the written terms of the hire-purchase agreement made clear that it was Patel's individual credit rating which counted. Secondly, the decision is also attractive as a practical matter. Under current practice, credit companies, which are physically absent when entering into such transactions, rely upon garage-owners to employ common sense and avoid becoming victims of fraudulent impersonation. It would be slower and more expensive for the credit company to meet each prospective purchaser before concluding this contract (however, MacMillan takes the opposite view, regarding the credit company's casual 'vetting procedure' as reckless).¹⁶⁶

10.33 *Apportionment: an unsuccessful judicial suggestion.* Devlin LJ had suggested in the *Ingram* case (1961), that apportionment might be considered as a solution to this problem.¹⁶⁷ This would involve the compromise solution of dividing the loss, perhaps in

158 (1878) 3 App Cas 454, HL.

159 [2003] UKHL 62; [2004] 1 AC 919, HL, at [69] and [70].

160 *Ibid.*

161 *Ibid.*, at [82]; and Law Reform Committee, *Transfer of Title to Chattels* (Twelfth Report of the Law Reform Committee, Cmnd 2958, 1966) (UK); Uniform Commercial Code (14th edn) (USA), 2-403.

162 [2004] 1 AC 919, HL, at [35]; a point made emphatically by Lord Denning MR in *Lewis v. Averay* [1972] 1 QB 198, 207, CA.

163 *Ibid.*, at [182].

164 [1950] 1 KB 671, 691, CA.

165 Law Reform Committee, *Transfer of Title to Chattels* (Twelfth Report of the Law Reform Committee, Cmnd 2958, 1966).

166 C. MacMillan, 'Mistake as to Identity Clarified?' (2004) 120 LQR 368, 373.

167 [1961] 1 QB 31, CA.

a discretionary way, between the victims. But the Law Reform Committee (1966) considered this suggestion to be impractical.¹⁶⁸

- 10.34 *Face-to-face dealings.* In this situation (a) a fraudulent impostor ('the rogue') tricks the vendor into parting with goods (most cases have concerned cars) on credit; the vendor normally receives a cheque which is not honoured; (b) the rogue's second victim is the innocent final purchaser who acquires a stolen vehicle (or other chattel). The first risk, at (a), can be easily evaded by insisting on clearance of the cheque before the goods are released to the purchaser. This might entail a delay in completion of the sale of several days. The second risk, at (b), is more insidious because there is no system of registration of title to chattels, including cars.
- 10.35 *Rescission by victim of fraud.* It is important to note that a contract can be rescinded (that is, avoided or set aside *ab initio*) if one party has been the victim of the other's fraudulent misrepresentation. In *Car & Universal Finance Co. Ltd v. Caldwell* (1965), the Court of Appeal held that rescission in this context does not require the victim to succeed in tracing the representor and informing him directly of this rescission.¹⁶⁹ That would often be a virtually impossible task. Instead, it is enough if the representee contacts the police and informs them that he has been the victim of such a fraud and wishes to trace the car and repossess it. Suppose A tells the police at 11.20 am that at 9.00 am that day he had been hoodwinked by B, a rogue, into accepting a cheque and handing over the car keys to B. If B had sold the vehicle at 11.19 am, the innocent sub-purchaser would acquire good title to the car; but, if the sub-sale took place later than A's notification to the police, the contract between A and B would have been rescinded already (at 11.20 am) so that it would not be possible for B to pass title to an innocent third party.
- 10.36 *Lewis v. Averay: preference for a voidable deal.* The Court of Appeal decision in *Lewis v. Averay* (1972)¹⁷⁰ was made in favour of the innocent sub-purchaser rather than the defrauded head vendor. During a face-to-face meeting, the vendor had been duped into believing that the purchaser, in fact an impostor, was a television actor; and this rogue then left the vendor's premises with the car keys and the car, in return for a worthless cheque. Once the cheque was dishonoured, and the fraud had become apparent, the rogue had already sold the car to an innocent third party. The Court of Appeal unanimously held that the latter acquired good title. This was because the head contract, between the duped

168 Law Reform Committee, *Transfer of Title to Chattels* (Twelfth Report of the Law Reform Committee, Cmnd 2958, 1966), paras. 9–12 (Committee considering that stumbling block is where C sells to rogue B, who sells to D1, who sells to D2).

169 [1965] 1 QB 525, CA; if the rogue sub-sells in the ordinary course of business, the sub-purchaser can receive good title under section 9 of the Factors Act 1889, or section 25 of the Sale of Goods Act 1979; *Newtons of Wembley Ltd v. Williams* [1965] 1 QB 560, CA; Cheshire, *Fifoot and Furmston's The Law of Contract* (15th edn, Oxford, 2007), 353; *Treitel* (12th edn, London, 2007), 9.085; J. Thornley, [1965] CLJ 24.

170 [1972] 1 QB 198, CA.

vendor and the rogue, had been voidable, and not absolutely void. Title had passed down this chain, therefore, to the innocent sub-purchaser.

- 10.37 The *Lewis* case was approved in the *Shogun* case (2004) (10.29 ff). Furthermore, the *Shogun* case treats the contrary result in *Ingram v. Little* (1961)¹⁷¹ (see the next paragraph) as wrong.
- 10.38 *Ingram v. Little* (1961): an aberrant decision. The approach and result explained above in *Lewis v. Averay* (1972) should be contrasted with a converse and earlier result, also decided by the Court of Appeal, in *Ingram v. Little* (1961),¹⁷² where the court resolved this triangular tangle in favour of the claimant, the duped head vendor.¹⁷³ This conflict of results is troublesome. But the *Ingram* case is now regarded as wrong. In *Lewis v. Averay* (1972),¹⁷⁴ the Court of Appeal disapproved the *Ingram* case. Furthermore, Lords Walker and Millett in the *Shogun* case (2004) thought that the *Ingram* case was wrongly decided because it conflicts with the ‘objective principle of agreement’.¹⁷⁵ That principle (3.57 ff) requires the law to regard C’s offer to sell the goods as directed at the flesh-and-blood person X, unless C can exceptionally show that he has made clear that he is intending only to deal with that person *on the assumption that he is truly the person whom he claims to be*.

In the *Ingram* case, after manifest hesitation, and following a feckless attempt at checking the purchaser’s identity, three elderly ladies sold a car to X. X had presented himself as ‘P. G. M. Hutchinson’ of Caterham, Surrey. Before concluding this deal, one of the ladies went to the Post Office. She verified that there was a Hutchinson at that address. This information mysteriously induced the ladies to believe that the man in their parlour was that very gentleman. Of course, this was a *non sequitur* (unfortunately Miss Marple had not been visiting for tea). They then handed the car keys to X in exchange for a worthless cheque. X soon re-sold the car to D who bought in good faith. A majority of the Court of Appeal declared that C had a good claim against the innocent sub-purchaser D in the tort of conversion because the contract between the elderly ladies and X had been void for error as to X’s identity.

- 10.39 The modern law can be stated as follows. If a face-to-face negotiation is to result in a judicial declaration that the supposed transaction is wholly void, the Court of Appeal’s decision in *Lewis v. Averay* (1972)¹⁷⁶ (for the facts of which, see 10.36) requires C, the head vendor, to show the following:

171 [1961] 1 QB 31, CA.

172 [1961] 1 QB 31, CA.

173 [1961] 1 QB 31, CA; this troublesome case is summarised by Lord Nicholls in *Shogun*, [2003] UKHL 62; [2004] 1 AC 919, HL, at [20] to [22].

174 [1972] 1 QB 198, 207, 208, CA (Lord Denning regarded the *Ingram* case, [1961] 1 QB 31, CA, as wrong; Phillimore LJ in the *Lewis* case thought the *Ingram* case was ‘special and unusual’, and Megaw LJ, [1972] 1 QB 198, 208, found the *Ingram* case difficult to understand).

175 *Shogun* case, [2003] UKHL 62; [2004] 1 AC 919, HL, at [185] and [110].

176 [1972] 1 QB 198, CA.

- (1) C intended to deal with Y (a real person or company) and not with X, the rogue;
- (2) X knew of C's intention and error;
- (3) C's error was crucial to his decision to contract;
- (4) C took reasonable steps to check X's identity (thinking X to be Y) before contracting with X.

As for element (1), it will be an uphill task for C, the head vendor, to establish that he was really intending only to deal with Y, rather than with X, the flesh-and-blood person standing before him (for this reason, the contract will be merely voidable for fraudulent misrepresentation and, provided the sub-sale precedes any effective rescission of the head-sale by the vendor, an innocent third party will acquire good title and so be protected against liability in the tort of conversion). C's task is an uphill one, but not impossible. As Lord Walker said in the *Shogun* case (2004), exceptionally C might show that he was proposing to deal with someone other than X, even though C and X stood face-to-face¹⁷⁷ (face-to-face dealings including telephone dealings, but not, of course, e-mail or postal communications).¹⁷⁸

10.40 Identity errors: summary. It is submitted that the key to this conundrum in the 'identity' cases is whether it is objectively clear that the target of A's dealings was 'Y', the represented identity, as distinct from X (the rogue's true identity).

- (1) Usually, in contracts formed by writing (which must include a transaction arising from e-mail or fax), the text of the communications will state that the parties to the intended transaction are to be 'A and Y'. In that situation, X's pretence that he is Y (or capable of acting as Y's agent) will not produce a valid consensus: only Y (or Y's authorised agent) can assent to the proposal for a contract with A. This analysis is clearly adopted by Lord Cairns LC in *Cundy v. Lindsay* (1878)¹⁷⁹ and by Lord Hobhouse in the *Shogun* case (2004).¹⁸⁰ The latter rightly founded this approach on the parol evidence rule (14.26). That rule prevents a person from adducing evidence to contradict the written contract's explicit identification of the contractual parties. If the written contract states that the other party is, and must be, 'Y', there can be no valid agreement if in fact Y was unaware of A and X's dealings and so could not have assented to a contract. In this situation, it is clear that the transaction is a nullity because of the complete absence of consent by Y.
- (2) If, unusually, the written contract does not identify the parties, it is possible that A might show that the identity of the other side was fundamental to A's wish to deal with the other side. Suppose that A sends or inserts by hand a note to the 'occupier' of a certain premises. Unknown to A, the occupier has changed: it is no longer Y but X. X purports to have accepted A's offer. In that situation, A must show that X

¹⁷⁷ [2003] UKHL 62; [2004] 1 AC 919, HL, at [187].

¹⁷⁸ *Ibid.*, at [18].

¹⁷⁹ (1878) 3 App Cas 454, HL.

¹⁸⁰ *Shogun* [2003] UKHL 62; [2004] 1 AC 919, HL, at [52] to [55], and also [45] to [49].

knew that A had not intended to deal with X and that Y's identity was crucial to A. Bramwell B in *Boulton v. Jones* (1857) supports the view that in this situation there will be no contract between A and X.¹⁸¹

Party A placed an order for goods. A thought he was dealing with Y, from whom A had previously received his supplies. But X was the new occupier of Y's premises, and in the same trade. X was aware of A's mistake because X had been Y's foreman. Y had owed A money and, therefore, A had a commercial interest in retaining a right of set-off *vis-à-vis* Y (set-off is, in this context, A's right to deduct from the value of Y's invoice for goods supplied the amount of the prior debt owed by Y to A). It seems that X must also have appreciated that A had this right of set-off. A had then used the goods before the confusion over X's identity revealed itself. It was held that X was not entitled to the price of goods from A.

- (3) There is an objective presumptive analysis in a face-to-face context (or perhaps when A is in telephone conversation with X) that A and X are dealing with each other, X's flesh-and-blood presence (or his speaking voice, where the phone is used) being all that counts.
- (4) In this face-to-face context, the objective presumptive analysis just mentioned is open to rebuttal if A has manifested a clear refusal to deal with X unless X is who he claims to be, namely, 'Y'. But this intention to deal solely with Y, rather than with X, must be clearly indicated. In the face-to-face context, *Lewis v. Averay* (1972)¹⁸² (for the facts of which, see 10.36) demonstrates that the courts are nowadays reluctant to make the finding that A only wished to deal with the prospective purchaser of a car if that purchaser is indeed the very same person he purports to be (namely, 'I will deal with you if and only if you are "Y", as declared'). But, as Lord Walker said in the *Shogun* case (2004), it is not impossible that A might succeed in establishing this.¹⁸³ In this regard, witnesses or paper indications will help (as will now be explained); otherwise, it is a question of A convincing the court on the basis of his unsupported oral evidence that he told X, a person who is unlikely to be traced after the fraud, that 'I am banking on you being Y'.
 - (a) It is obviously easier for A to convince the court that he had a special intention only to deal with 'Y', if there are witnesses to the transaction to corroborate A's assertion that he articulated his wish to deal only with Y.
 - (b) Another possibility is for a cautious vendor to make his assumption crystal-clear by composing a document, for the purchaser to sign, which states that it is agreed that the proposed deal is between A and 'Y', as X represents himself to be (although it will be rare for an ordinary person to be pedantic in this manner, commercial traders will be less reluctant to articulate their assumption, especially if large sums are at stake):

181 (1857) 27 LJ Ex 117, 119; *Cheshire, Fifoot and Furmston's The Law of Contract* (15th edn, Oxford, 2007), 311-12; R. Goff and G. H. Jones, *The Law of Restitution* (7th edn, London, 2007), 23-005.

182 [1972] 1 QB 198, CA.

183 [2003] UKHL 62; [2004] 1 AC 919, HL, at [86] and [87].

- (i) If the purchaser is in fact someone other than Y, A can justifiably declare that the contract is ineffective because there has been a failure by 'Y' to agree to the contract.
- (ii) The same result can be conceptualised in another way: by contending that this written contract makes clear that it is a condition precedent to the transaction that Y should be the person actually present at the time of this deal, and thus the true and only party to the proposed deal with party A.

Of course, to avoid these problems, sensible vendors will not part with their property until cash payment has been received in full, or payment by cheque has cleared.

Chapter contents

1. Introduction *para.* 11.01
2. Duress *para.* 11.02
3. Undue influence *para.* 11.23
4. Unconscionability or exploitation *para.* 11.36
5. Substantively unfair bargains *para.* 11.40
6. No doctrine of 'inequality of bargaining power' *para.* 11.42

11

Duress, undue influence and unconscionability

1. INTRODUCTION

11.01 Summary of main points

- (1) *Duress*. This involves the application of illegitimate pressure so that the relevant contract or contractual modification is unsafe and should be set aside. The pressure will normally take the form of a threatened legal wrong (crime, tort, breach of contract, etc.). Exceptionally, it might be the threat of a lawful act (such as reporting a person to the police or some other authority). In the latter type of case, the court might regard the threat as 'illegitimate', that is, an unacceptable or morally reprehensible use of pressure; but this can only involve a value judgement because, *ex hypothesi*, the threat was not to break the law.
- (2) *Undue influence*. This is an equitable doctrine. 'Actual undue influence' is broader than coercion, although it can take the form of coercion. If actual undue influence is shown, there is no need to show that the transaction is objectively 'unfair' and 'unbalanced'. However, the more common situation is that undue influence involves abuse of a relationship by someone occupying a superior or dominant position. Plainly, unequal relationships include solicitor/client, teacher/pupil, spiritual advisor/follower, trustee/beneficiary. Here, the law acknowledges that the danger of abuse exists. To this extent, the law speaks of 'presumed undue influence'. In other situations, the claimant must show that, on the particular facts of the case, he 'looked up to' and so placed 'trust and confidence' in the other.
- (3) *Unconscionability or exploitation*. This is another equitable doctrine. Its essence is that a stronger party has taken unacceptable advantage of the other party's weakness or vulnerability in an exceptionally 'shocking' fashion. As a result, the relevant transaction

is severely weighted in favour of the stronger party. Even so, the transaction might be upheld if the claimant received independent legal advice before acceding to the agreement, and the court is satisfied that the decision to contract was made in a free and informed way. Despite its long history, this doctrine remains in a state of development. Case law will need to illuminate further which types of personal vulnerability count for the purpose of this doctrine, and what degree of 'hardship' is required.

- (4) *Survey of the doctrines.* In principle (in fact, as will be noted, only categories (a) to (c) are subject to judicial regulation), the law might intervene to invalidate a contract, or a particular term (or a gift), on a number of possible grounds: (a) 'duress', that is, coercion; (b) 'undue influence', that is, abuse of a position of trust or dependence; (c) 'unconscionable conduct' or 'exploitation' of another's weakness; (d) 'substantive unfairness', that is, intrinsically exorbitant or harsh bargains or clauses; and (e) a combination of substantive unfairness and 'inequality of bargaining power'. As for category (d), 'substantive unfairness', such a complaint would consist solely of the fact that the agreement as a whole, or a particular term or clause, is intrinsically unacceptable because it is wholly lopsided. However, English law has not embraced such a general doctrine: substantive unfairness is not a general basis of judicial or statutory intervention (for exceptions, see 11.41). Nor has English law adopted 'inequality of bargaining power', category (e), as a free-standing basis for invalidating contracts. Such an approach had been suggested by Lord Denning MR in his minority judgment in *Lloyds Bank v. Bundy* (1975),¹ but this has not been accepted in later cases as the basis for judicial intervention (11.42).² The two main objections to Lord Denning's suggestion for change are: first, such a sweeping doctrine would render the law uncertain; secondly, Parliament is better placed than the courts to implement such social and economic regulation. In fact, some legislation is clearly a response to acute inequality of bargaining power in particular contexts, notably the Unfair Terms in Consumer Contracts Regulations 1999 (15.33) and the consumer credit legislation.³

The topics in this chapter have stimulated much academic literature. These are some of the more interesting.

1 [1975] QB 326, 337–40, CA.

2 Notably by Lord Scarman in *National Westminster Bank v. Morgan* [1985] AC 686, 708, HL.

3 Sections 140A and 140B of the Consumer Credit Act 1974 (inserted by section 19 of the Consumer Credit Act 2006), imposing a criterion of unfairness in favour of the debtor.

Coercion

- A. Burrows, *The Law of Restitution* (2nd edn, London, 2002), chapter 5
- P. Birks, 'The Travails of Duress' [1990] LMCLQ 342
- J. P. Dawson, 'Economic Duress: An Essay in Perspective' (1947) 45 *Michigan Law Review* 253
- P. Winder, 'The Equitable Doctrine of Pressure' (1962) 82 LQR 165

Undue influence and unconscionability

- M. Oldham [2002] CLJ 29 (a case note on *Etridge (No. 2)*)
- D. O'Sullivan, (2002) 118 LQR 337 (a case note on *Etridge (No. 2)*)
- P. Birks and N. Y. Chin, 'On the Nature of Undue Influence', in J. Beatson and D. Friedmann (eds.), *Good Faith and Fault in Contract Law* (Oxford, 1995), 57, especially at 57–60, 63–5, 85–8, 92–7; for a reply to Birks and Chin, see R. Bigwood, *Exploitative Contracts* (Oxford, 2003), 467 ff; for a rejoinder, see P. Birks [1997] *Restitution Law Review* 72, 76 n. 20; Birks and Chin's argument has not been adopted: for further criticism, see the 1998 article by Capper listed below
- P. Birks, 'Undue Influence as Wrongful Exploitation' (2004) 120 LQR 34–7 (for a reiteration of his 'claimant-sided theory' stated in the article by Birks and Chin listed above)
- N. Bamforth, 'Unconscionability as a Vitiating Factor' [1995] LMCLQ 538
- D. Capper, 'Undue Influence and Unconscionability: A Rationalisation' (1998) 114 LQR 479, especially 492–504
- D. Capper, 'The Unconscionable Bargain in the Common Law World' (2010) 126 LQR 403
- M. Chen-Wishart, 'Undue Influence: Beyond Impaired Consent and Wrongdoing Towards a Relational Analysis', in A. Burrows and A. Rodger (eds.), *Mapping the Law: Essays in Memory of Peter Birks* (Oxford, 2006)
- M. Chen-Wishart, 'Undue Influence: Vindicating Relationships of Influence' [2006] CLP 231
- S. Waddams, 'Unconscionability in Contracts' (1976) 39 MLR 369

Substantive unfairness

- S. Smith, 'In Defence of Substantive Unfairness' (1996) 112 LQR 138

Inequality of bargaining power

- M. Trebilcock, 'The Doctrine of Inequality of Bargaining Power: Post-Benthamite Economics in the House of Lords' (1976) 26 *University of Toronto Law Journal* 359

General

- R. Bigwood, *Exploitative Contracts* (Oxford, 2003) (a long and detailed examination)

History

- J. L. Barton, 'The Enforcement of Hard Bargains' (1987) 103 LQR 118

2. DURESS⁴

- 11.02 Duress is a common law doctrine (equity's doctrine of coercion has now been superseded by common law).⁵ The essence of 'duress' is improper pressure, and this must be sufficiently powerful and influential so as to render consent legally unsustainable. Such coercion can involve direct force (violence against a person, or harm to his property or his commercial interests); or coercion can involve the threat of personal violence, or of material or economic harm, or of harm to a person's personal or family reputation.⁶ As Lord Devlin said:

All that matters to the plaintiff is that, metaphorically speaking, a club has been used. It does not matter to the plaintiff what the club was made of – whether it is a physical club or an economic club or otherwise an illegal club.⁷

It is now usual to arrange duress under three categories: duress as to person; duress as to goods; and economic duress (see 11.12). Because threats can concern matters of personal or family reputation, however, this tripartite classification is not exhaustive.

- 11.03 Duress does not extinguish contractual consent but merely vitiates it. Thus, a coerced party is psychologically aware of the transaction: he is neither mistaken about what he is doing, nor is he an automaton. In fact, he is all too 'painfully' or vividly aware of what, contrary to his wishes, he is being coerced to do. The coerced person's consent is 'vitiating' because he was not psychologically 'free' when deciding to enter the relevant agreement. The Latin tag for this constrained act of contracting is *coactus volui*, 'I volunteered to act, having been compelled to do so.'

- 11.04 The four components of duress are:

- (1) pressure applied or harm threatened;
- (2) improper nature of the direct pressure or threatened harm (unlawful conduct threatened or a threat of an otherwise 'illegitimate' nature);

⁴ In addition to the literature cited at 11.15, see also R. Bigwood, *Exploitative Contracts* (Oxford, 2003); N. Enonchong, *Duress, Undue Influence and Unconscionable Dealing* (London, 2006); R. Goff and G. H. Jones, *The Law of Restitution* (7th edn, London, 2007), chapter 10; A. Burrows, *The Law of Restitution* (2nd edn, London, 2002), chapter 5; G. Virgo, *Principles of the Law of Restitution* (2nd edn, Oxford, 2006), chapter 9; J. Beatson, *Use and Abuse of Unjust Enrichment* (Oxford, 1991), 95–136, and, earlier, [1974] CLJ 94; P. Birks, [1990] LMCLQ 342; J. P. Dawson, (1947) 45 *Michigan Law Review* 253; R. Halson, (1991) 107 LQR 649; A. Phang, (1992) 5 *Journal of Contract Law* 147, and (1990) 53 MLR 107, and [1997] *Restitution Law Review* 53–65; S. A. Smith, [1997] CLJ 342–73; for interesting comparative discussion, see J. du Plessis, in H. MacQueen and R. Zimmermann (eds.), *European Contract Law: Scots and South African Perspectives* (Edinburgh, 2006), chapter 6.

⁵ Cf *Williams v. Bayley* (1866) LR 1 HL 200 (classified by Lord Denning MR, in *Lloyds Bank Ltd v. Bundy* [1975] QB 326, 338, CA, as a case of 'undue pressure', citing Lord Westbury, (1866) LR 1 HL 200, 218–19); P. Winder (1939) 3 MLR 97, 110 ff and (1962) 82 LQR 165; *Kaufman v. Gerson* [1904] 1 KB 591, CA; *Mutual Finance Ltd v. Wetton & Sons Ltd* [1939] 2 KB 389, Porter J; *D & C Builders v. Rees* [1966] 2 QB 617, 625, CA, per Lord Denning MR.

⁶ Cf *Kaufman v. Gerson* [1904] 1 KB 591, CA (threat to prosecute husband, which would produce infamy for his wife's family and children).

⁷ *Rookes v. Barnard* [1964] AC 1129, 1209, HL, per Lord Devlin (spoken in context of tort of intimidation; and approving Hamson's analysis, [1961] CLJ 191, 192).

- (3) the objective potency of pressure (not every degree of pressure will suffice); and
- (4) the causal impact of the pressure (the pressure must have had the right degree of influence on this party).

These factors will be explained below.

11.05 It is helpful to consider the following judicial definitions. In *Universe Tankships Inc. of Monrovia v. International Transport Workers Federation* ('*The Universe Sentinel*') (1983), Lord Scarman said:⁸

[There are] two elements in the wrong of duress: (1) pressure amounting to compulsion of the will of the victim; and (2) the illegitimacy of the pressure exerted ... The classic case of duress is, however, not the lack of will to submit but the victim's intentional submission arising from the realisation that there is no other practical choice open to him.

He added:

In determining what is legitimate two matters may have to be considered. The first is as to the nature of the pressure. In many cases this will be decisive, though not in every case. And so the second question may have to be considered, namely the nature of the demand which the pressure is applied to support ... [T]he law regards the threat of unlawful action as illegitimate, whatever the demand. Duress can, of course, exist even if the threat is one of lawful action: whether it does so depends upon the nature of the demand.

And, in *Dimskal Shipping Co. SA v. International Transport Workers Federation* ('*The Evia Luck No. 2*') (1992), Lord Goff said:

[E]conomic pressure may be sufficient to amount to duress ... provided at least that the economic pressure may be characterised as illegitimate and has constituted a significant cause inducing the plaintiff to enter into the relevant contract.⁹

11.06 *Implicit or overt pressure.* There must be either pressure, directly applied, or harm threatened. A 'threat' is normally explicit, but it might be implicit.¹⁰ But, especially in the context of contractual renegotiation, implicit threats should not be found too readily (11.15). Thus, a party's statement that he is unwilling to continue performance need not constitute an implicit threat. Instead, it might be merely an honest and non-coercive attempt to explore the chance of a compromise arrangement.

⁸ [1983] 1 AC 366, 400–1, HL.

⁹ [1992] 2 AC 152, 165G, HL.

¹⁰ *Williams v. Bayley* (1866) LR 1 HL 200 (father executed mortgage in favour of bank because latter intimated that son might be prosecuted for forgery; Lord Cranworth LC found an implied threat); and see *Mutual Finance Ltd v. Wetton & Sons Ltd* [1939] 2 KB 389, Porter J (implicit threat to prosecute family member, X, for forgery; X's father and brother entering transaction to avert scandal).

11.07 *Target of threat and maker of the threat.* The target of the threat is normally the contracting party, who now seeks to set aside the agreement. But it might be directed at third parties towards whom the allegedly coerced party has a special responsibility or attachment.¹¹ Similarly, the threatening party is normally the other contracting party. But a third party, T, can make a threat against A, one of the contracting parties. If T is threatening A, the contract will be voidable by A only if B, the other prospective party to the transaction, was aware of this pressure, or B was perhaps constructively aware (as adopted by UNIDROIT's *Principles of International Commercial Contracts* (2004)).¹²

11.08 *Improper nature of the threat.* The threatened act must be either *unlawful* (a crime, tort or breach of contract) or *illegitimate*.

- (1) *Unlawful.* The fact that the threatened conduct or pressure is unlawful renders it automatically illegitimate. In '*The Universe Sentinel*' (1983), Lord Scarman said:¹³ '[T]he law regards the threat of unlawful action as illegitimate, whatever the demand. Duress can, of course, exist even if the threat is one of lawful action: whether it does so depends upon the nature of the demand.' Because a breach of contract is an unlawful act, it follows that a threat of a breach of contract is necessarily the threat of an unlawful act and hence illegitimate. This is the correct and authoritative approach. Admittedly, Dyson J in *DSND Subsea Ltd v. Petroleum Geo-Services ASA* (2000) suggested that a threat of a breach of contract is not necessarily unlawful.¹⁴ But the better view is that every breach of contract is necessarily unlawful. The test of 'illegitimacy' should not be used to 'legitimise' such a threat. This point is further examined at 11.17 ff.
- (2) *Illegitimate.* Even if the threatened act is not unlawful, it is possible that it might nevertheless be regarded by the court as illegitimate. Birks notes: '[I]f ... lawful pressures are always exempt, those who devise outrageous but technically lawful means of compulsion must always escape [liability] until the legislature declares the abuse unlawful.'¹⁵ As Birks and Chin observe, the word "illegitimate" has been chosen precisely because it has softer edges than, say, "unlawful".¹⁶

As regards the relationship between these two categories, there is no need to consider category (2) if category (1) is satisfied.

11 *Ibid.*

12 UNIDROIT's *Principles of International Commercial Contracts* (2nd edn, Rome, 2004), Article 3.11(2); M. J. Bonell (ed.), *The UNIDROIT Principles in Practice: Case Law and Bibliography on the UNIDROIT Principles of International Commercial Contracts* (2nd edn, Ardsley, NY, 2006), 211; S. Vogenauer and J. Kleinheisterkamp (eds.), *Commentary on the UNIDROIT Principles of International Commercial Contracts* (Oxford, 2009), 457.

13 *Universe Tankships Inc. of Monrovia v. International Transport Workers Federation* [1983] 1 AC 366, 400–1, HL.

14 [2000] BLR 530; noted by R. Bigwood, (2001) 117 LQR 376.

15 P. B. H. Birks, *An Introduction to the Law of Restitution* (Oxford, 1989), 177.

16 P. B. H. Birks and N. Y. Chin, 'On the Nature of Undue Influence', in J. Beatson and D. Friedmann (eds.), *Good Faith and Fault in Contract Law* (Oxford, 1995), 64.

- 11.09 *Category (2): lawful threat or pressure: no improper duress in a particular commercial context.* The Court of Appeal's decision in *CTN Cash & Carry Ltd v. Gallaher* (1994) illustrates that as between commercial parties the courts must assess the facts to discover whether a threatened 'lawful act' constitutes an illegitimate threat in that particular context.¹⁷ On the facts of that case, the threat was declared not to be illegitimate. Steyn LJ emphasised three points: first, the need for certainty in the commercial sphere; secondly, the importance of maintaining closed transactions; finally, the defendant's good faith in making its demand. He said: 'The aim of our commercial law ought to be to encourage fair dealing between parties. But it is a mistake for the law to set its sights too highly when the critical enquiry is not whether the conduct is lawful but whether it is morally or socially unacceptable.'¹⁸

In *CTN Cash & Carry Ltd v. Gallaher* (1994), the defendant was a manufacturer of cigarettes. The claimant regularly bought these in bulk for distribution to retailers. A consignment was delivered ostensibly to the claimant, but in fact to the wrong warehouse, that is, to the claimant's Burnley warehouse rather than to its Preston warehouse. A third party stole the goods. There was a dispute whether the claimant should pay for them. The defendant claimed in good faith (although erroneously, as conceded during the litigation) that the goods had been at the claimant's risk and, therefore, that the claimant was obliged to pay. The claimant acceded to this request for payment only after the defendant threatened a lawful act, namely, to withdraw its 'credit facility' on future sales, that is, to insist on cash payment 'up-front' before making future deliveries. There was no obligation that the defendant should continue supplying goods on this credit basis. Although not unlawful, the threat was a potent one. Nevertheless, the Court of Appeal held that the agreement to pay was not voidable for duress. On these facts, the threat was treated as being not illegitimate.

- 11.10 *No improper pressure suffered by SAS soldier: in R v. Her Majesty's Attorney-General for England and Wales* (2003),¹⁹ a soldier had signed a confidentiality clause as a condition of remaining with the elite SAS regiment. He later challenged the validity of that agreement on the basis that it resulted from duress or undue influence. The Privy Council unanimously rejected the duress (and by a majority it also rejected the undue influence plea: 11.29). The duress plea failed because the threat was held to be neither unlawful nor illegitimate:

There was no order in the sense of a command which created an obligation to obey under military law. Instead, R was faced with a choice which may have constituted 'overwhelming pressure' but was not an exercise by the Ministry of Defence of its legal powers over him. The legitimacy of the pressure therefore falls to be examined by normal criteria and as neither of the courts in New Zealand considered either the

¹⁷ [1994] 4 All ER 714, CA.

¹⁸ *Ibid.*, at 719.

¹⁹ [2003] UKPC 22; [2003] EMLR 24, at [15] ff.

threat to be unlawful or the demand unreasonable, it follows that the contract was not obtained by duress.²⁰

- 11.11 *Objective potency of pressure.* Adopting the objective standard of the reasonably robust person, the threat must be potent enough to give the victim *no effective choice but to give in*.²¹

Some might dispute whether this element is required.²² However, it is submitted that this requirement is sound. Without this, duress would be unacceptably broadened. It is pleasing to note that this requirement has been adopted by UNIDROIT's *Principles of International Commercial Contracts* (2004), a 'soft law' document of considerable influence and growing authority (see 21.01 ff for a general discussion of this and other 'soft law' codes).²³

On the question whether the relevant pressure deprived the coerced party of any real alternative other than to submit to the threat, see the discussion at 11.20 of the following cases: (1) *B & S Contracts & Design Ltd v. Victor Green Publications Ltd* (1984);²⁴ (2) *Atlas Express Ltd v. Kafco (Importers and Distributors) Ltd* (1989);²⁵ and (3) *Adam Opel GmbH v. Mitras Automotive UK Ltd* (2008).²⁶

- 11.12 *Causal impact of the pressure.* The obvious question is this: 'Did the threat make all the difference, so that without it the coerced party would not have given consent?' Such a test, the so-called 'but for' or 'decisive influence' test, applies to economic duress²⁷ and probably to duress as to goods (see 11.02 for the threefold distinction of 'duress as to person', 'duress as to goods' and 'economic duress'). But, according to the Privy Council in *Barton v. Armstrong* (1976),²⁸ this test does *not* apply to duress as to the person (on the parallel approach in respect of fraudulent misrepresentation, see 9.04). Instead, in the case of duress to the person, it is enough that the coerced party was influenced by the duress and did not choose simply to shrug it off. According to this decision, duress to the person will invalidate a transaction even if the coerced party would have entered into the same transaction, and on the same terms, in the absence of this duress. It is enough that the coercion caused some mental disturbance, even though causally it was not decisive.

20 *Ibid.*, at [20].

21 *B & S Contracts & Design Ltd v. Victor Green Publications Ltd* [1984] ICR 419, 428, CA, *per* Kerr LJ; J. O'Sullivan and J. Hilliard, *The Law of Contract* (4th edn, Oxford, 2010), 11.22, call this the 'objective' aspect of coercion.

22 Cf Mance J in the *Huyton* case, [1999] 1 Lloyd's Rep 620, 638.

23 UNIDROIT's *Principles of International Commercial Contracts* (2nd edn, Rome, 2004), Article 3.9, referring to a threat 'so imminent and serious as to leave [the threatened person] no reasonable alternative'; M. J. Bonell (ed.), *The UNIDROIT Principles in Practice: Case Law and Bibliography on the UNIDROIT Principles of International Commercial Contracts* (2nd edn, Ardsley, NY, 2006), 205; S. Vogenauer and J. Kleinheisterkamp (eds.), *Commentary on the UNIDROIT Principles of International Commercial Contracts* (Oxford, 2009), 442.

24 [1984] ICR 419, CA.

25 [1989] QB 833, Tucker J; noted by D. Fleming, [1989] CLJ 362.

26 [2008] EWHC 3205 (QB); [2008] Bus LR D55.

27 *Huyton SA v. Peter Cremer GmbH & Co.* [1999] 1 Lloyd's Rep 620, 636, Mance J.

28 [1976] AC 104, PC.

Barton v. Armstrong (1976) concerned a threat to assassinate the claimant. It was established by the Australian trial judge (Street J) and upheld by the New South Wales appeal court, that the victim of this threat had already determined to enter the relevant transactions for reasons quite independent of the unlawful threat. If this was so, duress had no relevant impact at all: it was causally irrelevant.

Lords Wilberforce and Simon of Glaisdale in the Privy Council agreed that the legal test should be not whether the contract would have been formed on the same terms even if there had been no coercion, but whether the coercion had, as it were, been a psychological damp squib, having no impact at all on the threatened party. On that question of fact, they dissented from the majority of the Privy Council. In the view of Lords Wilberforce and Simon, the Privy Council should have affirmed the finding of 'no duress', because the Australian courts' finding of fact was that duress had formed no part at all of the motivation to enter the contract.

It is submitted that the 'but for' or 'decisive influence' test should be applied uniformly to all three categories of duress. Even if the victim has been frightened by a violent threat, the transaction should not be invalidated if it is plain that it made no difference to his decision both to contract and to conclude the deal on the very same terms.

- 11.13 *Nature of contractual invalidity.* Lord Scarman declared in *Pao On v. Lau Yiu Long* (1980) that duress renders the contract voidable, at least in the context of 'economic duress' (and, almost certainly, duress as to goods).²⁹ The three consequences of treating the transaction as voidable, as distinct from void *ab initio*, are: (1) a sub-purchaser, if he receives in good faith and without notice, will acquire good title; (2) the coerced party also has the choice whether to affirm or set aside the relevant coerced transaction (see the parallel points in the context of mistake as to the person, and the *Cundy v. Lindsay* and *Shogun* cases, at 10.23 ff); (3) during rescission, the parties' position can be adjusted (9.18 ff); the flexible process of rescission, pioneered by equity, now extends to the common law doctrine of duress.³⁰

It is submitted that, in the interest of consistency, the 'voidable' analysis should be applied even where the threat or pressure involves direct personal violence. But there are loose ends which will require reconsideration. First, Lord Cross' majority opinion in the Privy Council in *Barton v. Armstrong* (1976)³¹ contains the unreasoned suggestion that a contract might be wholly *void* if the duress employed involves threatened, or actual, personal violence. Secondly, the anomalous common law doctrine of *non est factum* (10.22) will apply to a case where the signatory has been the victim of direct force (as when the contracting party's act of signature is the result of his hand being moved against his will

29 *Pao On v. Liu Yiu Long* [1980] AC 614, PC (cf Lord Cross' earlier reference in *Barton v. Armstrong* [1976] AC 104, 120, PC, to a threat as to person rendering the contract 'void so far as concerns him' is ambiguous on this point).

30 *Halpern v. Halpern* (No. 2) [2007] EWCA Civ 291; [2008] QB 195, at [61] and [76] (rescission for duress: need for claimant to give credit for benefits received: 'counter-restitution').

31 [1976] AC 104, 109, 120, PC.

by a person who is applying direct force, or perhaps a gun is placed to his or her loved one's head), and that doctrine renders the relevant transaction *void*.³²

- 11.14 *Defence of affirmation*. If the coerced party affirms the contract, after the relevant coercion has ceased to influence him, he will lose the chance to set aside the contract. If affirmation is disputed, Mocatta J in '*The Atlantic Baron*' (1979) held that the following objective approach will be adopted:³³ whether the coerced party's overt acts or words indicated that he was affirming the contract. And so that party's 'secret mental reservation' will be irrelevant.
- 11.15 *Duress and renegotiation of contracts*.³⁴ Party A might seek either to increase the remuneration for a job ('increasing pact') or, where A is a debtor, try to procure B's agreement to reduce or cancel the debt ('decreasing pact') (on these categories of renegotiation, see 5.33 to 5.63). The more important context concerns 'increasing pacts', that is, a contractual modification under which B promises to pay A more money. There are various ways in which such a renegotiation can arise:
- (1) *The other party initiates renegotiation*. B might take the initiative and call in A to discuss what can be done to improve A's performance or to ensure that A performs on time.
 - (2) *Non-coercive inquiry*. A might gently and courteously broach the question of revising the terms without making an explicit or veiled threat not to proceed unless better terms are obtained.
 - (3) *Overt threats*. A might broach the same issue by making a clear threat not to proceed unless the terms are revised to suit A.
 - (4) *Veiled threats*. A might achieve the same level of coercion without using clear menaces, because it is clear to A and B that the former is implicitly threatening to 'down tools', or the commercial equivalent.
- 11.16 Only in fairly recent times has the doctrine of duress become significant in this context. Economic duress was first recognised by Kerr J in '*The Siboen and the Sibotre*' (1976).³⁵ At that time, the doctrine of consideration (the rule in *Stilk v. Myrick* (1809); see 5.37)³⁶ dominated this context: a promise (*whether or not coerced*) to pay more for the same job,

32 R. Goff and G. H. Jones, *The Law of Restitution* (7th edn, London, 2007), 10.001; however, *non est factum* (10.22) is in tension with the dominant principle of 'objective consent' (3.57 ff); and it is submitted that the law should be slow to carve out a special and exceptional category of 'void' transactions.

33 *North Ocean Shipping v. Hyundai Construction Co. Ltd* ('*The Atlantic Baron*') [1979] QB 705, Mocatta J.

34 P. Birks, [1990] LMCLQ 342; J. Beatson, *Use and Abuse of Unjust Enrichment* (Oxford, 1991), 95–136; R. Goff and G. H. Jones, *The Law of Restitution* (7th edn, London, 2007), 10–25 ff; A. Burrows, *The Law of Restitution* (2nd edn, London, 2002), 224–34; G. Virgo, *Principles of the Law of Restitution* (2nd edn, Oxford, 2006), 203 ff; M. Chen-Wishart, in J. Beatson and D. Friedmann (eds.), *Good Faith and Fault in Contract Law* (Oxford, 1995), 142–3; R. Halson, (1991) 107 LQR 649 and R. Halson, *Contract Law* (London, 2001), 337 ff; E. MacDonald, [1989] JBL 460.

35 [1976] 1 Lloyd's Rep 293, Kerr J; noted by J. Beatson, (1976) 92 LQR 496.

36 (1809) 2 Camp 317, Lord Ellenborough CJ.

or otherwise to improve A's terms, would not be supported by consideration because the proposed new deal would not involve A incurring 'detriment'. But extension of duress to encompass economic threats, following Kerr J's pioneering decision in *'The Siboen and the Sibotre'* (1976),³⁷ left the path free for a recrafting of the consideration doctrine in the context of 'increasing pacts'³⁸ (see 5.34, 5.40, on *Williams v. Roffey & Nicholls* (1991), where no explicit or implicit threat was made).³⁹ As a result, A (the beneficiary of a promise to pay more for essentially the same performance as A had already promised) can now invoke the concept of a requested 'practical benefit' (essentially, A's willingness to proceed with the same job, rather than leaving B 'high and dry'), and this will satisfy the consideration requirement. Unless the relevant job has already been completed, so that there is no scope even for this very generous notion of 'practical benefit', a promise to pay more (an 'increasing pact') will be enforceable, in the absence of 'fraud' or 'duress'.

- 11.17 If the law of duress in respect of contractual modification is to be predictable, it must be grounded in settled and clear principles. One cardinal principle is that a threatened breach of contract is the threat of an intrinsically unlawful act; and thus this type of threat is necessarily 'improper' or 'illegitimate'. However, this orthodoxy was unconvincingly challenged by Dyson J in *DSND Subsea Ltd v. Petroleum Geo-Services ASA* (2000), who suggested that a threat of a breach of contract is not necessarily unlawful:⁴⁰

In determining whether there has been illegitimate pressure, the court takes into account a range of factors. These include whether there had been an actual or threatened breach of contract; whether the person allegedly exerting the pressure had acted in good or bad faith [on this point, see the *Huyton* case (1999), examined in the text below at the next note]; whether the victim had any realistic practical alternative but to submit to the pressure; whether the victim protested at the time; and whether he affirmed and sought to rely on the contract.

But (see further 11.19) this is simply wrong. Dyson J's use of the word 'illegitimate' in this passage conflates the questions: (1) Was pressure applied or a threat made? (2) Did this involve an actual or threatened breach of contract? (3) Did the coerced party have a realistic practical alternative? (4) Did he in fact submit? (5) Did he affirm the contract after the pressure had ceased to operate?

A *dictum* of Mance J in *Huyton SA v. Peter Cremer GmbH & Co.* (1999) unfortunately supports Dyson J's confusing and fallacious presentation of the law. In the *Huyton* case Mance J said:⁴¹

Even in cases where the pressure relied on is an actual or threatened breach of duty, it seems to me better not to exclude the possibility that the state of mind of the person

37 [1976] 1 Lloyd's Rep 293, Kerr J; noted by J. Beatson, (1976) 92 LQR 496.

38 Their siblings being 'decreasing pacts', 5.34 ff: the upwards or downwards 'pact' terminology is adopted with gratitude from G. H. Treitel, *Some Landmarks of Twentieth Century Contract Law* (Oxford, 2002), 11.

39 [1991] 1 QB 1, CA.

40 [2000] BLR 530, at [131]; noted by R. Bigwood, (2001) 117 LQR 376.

41 [1999] 1 Lloyd's Rep 620, 637, Mance J.

applying such pressure may in some circumstances be significant, whether or not the other innocent party correctly appreciated such state of mind. 'Never' in this context also seems too strong a word.

The better and orthodox view is that a threat to breach a contract is illegitimate, even if the coercing party believed he had a legal right to make the threat. What counts is that the threat in fact involved a breach of contract. If so, the threat is illegitimate.

11.18 Some commentators have also unconvincingly challenged (11.19) the orthodox view that the threat of a breach of contract is unlawful and, therefore, necessarily illegitimate. Thus, Burrows and Halson suggest that the law of duress should not invalidate a renegotiation, even if it was the result of significant pressure, if (1) the new agreement rectifies an imbalance which has occurred since the contract's formation (and without A's fault);⁴² or (2), as Burrows contends, if the renegotiation stems from the originally 'unfair' terms of the contract.⁴³ S. A. Smith similarly proposes such a nuanced approach.⁴⁴

11.19 But it would be surprising, and regrettable, if this approach were to be judicially affirmed. It is submitted that neither (1) nor (2) should be accepted. It cannot be commercially acceptable for a contractor who runs into trouble, or who has failed to do his initial sums correctly, to be able to uphold a 'rise' in remuneration secured only after coercing his contractual adversary. The coercing party's position is unmeritorious. After all, he had threatened to breach the contract, and such breach would be an unlawful act. It is wrong to treat a threatened breach of contract as 'legitimate' because the coercing party has a 'good faith' interest in preserving or enhancing his commercial interests. Instead, the better view is that, as Bigwood rightly says, a threatened breach of contract is necessarily illegitimate, because it is a threat of an unlawful act:⁴⁵ 'Although breach of contract is perhaps not as serious a matter as (some) crimes and torts, to suggest that it may sometimes be "not illegitimate" for one to breach one's contracts (in support of one's demands) is effectively to deny that contracts create true legal rights.' O'Sullivan and Hilliard (2010),⁴⁶ Macdonald (1983 and 2007)⁴⁷ and Tan share Bigwood's opinion.⁴⁸ Given, therefore, (1) the improper nature of a threatened breach of contract, the real points of focus should be on these further questions: (2) Can the relevant party show that the other made a threat, normally expressly, but sometimes impliedly? (3) Was the threat severe enough to leave him no practical choice other than to submit ('objective potency')? (4) Did the threat influence the targeted party ('causal impact')?

42 A. S. Burrows, *The Law of Restitution* (2nd edn, London, 2002), 233; R. Halson, *Contract Law* (London, 2001), 344 (Burrows' argument has been doubted by Mance J, in *Huyton SA v. Peter Cremer GmbH & Co.* [1999] 1 Lloyd's Rep 620, 637, who said: 'This suggestion, too, is by no means uncontentious').

43 A. S. Burrows, *The Law of Restitution* (2nd edn, London, 2002), 233.

44 Atiyah's *Introduction to the Law of Contract* (6th edn, Oxford, 2006), 268–71.

45 R. Bigwood, (2001) 117 LQR 376, 379.

46 *The Law of Contract* (4th edn, Oxford, 2010), 11.16.

47 E. Macdonald, 'Duress by Threatened Breach of Contract' [1989] JBL 460, at 463, 473; L. Koffman and E. Macdonald, *The Law of Contract* (6th edn, Oxford, 2007), 14.9.

48 D. S. Tan, (2002) 18 Const LJ 86, 91–2.

11.20 *Overwhelming commercial pressure during a renegotiation.* Three examples will be given here, although there are many other cases:⁴⁹ (1) *B & S Contracts & Design Ltd v. Victor Green Publications Ltd* (1984);⁵⁰ (2) *Atlas Express Ltd v. Kafco (Importers and Distributors) Ltd* (1989);⁵¹ and (3) *Adam Opel GmbH v. Mitras Automotive UK Ltd* (2008).⁵²

- (1) In *B & S Contracts & Design Ltd v. Victor Green Publications Ltd* (1984),⁵³ the Court of Appeal held that contractors had applied such pressure that the other party had no practical alternative other than to give in to the threat of breach of contract and to pay a sum under commercial extortion. P agreed to erect stands for D at Olympia (an indoor exhibition centre in London) under a contract with a *force majeure* clause (see generally 12.02 at (16)), which provided that the contract was subject to variation or cancellation in the event of a strike. P intended to use staff from their insolvent subsidiary in Wales. But these workers refused to co-operate with P until their (unjustified) demand for severance pay had been satisfied. P told D that the contract would be cancelled unless D paid an additional sum to meet the workers' demands. D paid the sum and the contract was performed. The Court of Appeal held that D was entitled to deduct this sum from the contract price payable to P because it had been procured by P's economic duress. Kerr LJ said:⁵⁴

[A] threat to break a contract unless money is paid by the other party can, but by no means always will, constitute duress. It appears from the authorities that it will only constitute duress if the consequences of a refusal would be serious and immediate so that there is no reasonable alternative open, such as by legal redress, obtaining an injunction, etc.

- (2) In *Atlas Express Ltd v. Kafco (Importers and Distributors) Ltd* (1989), Tucker J held that a carrier's renegotiation of the carriage rate had been procured by economic duress.⁵⁵ The defendant had agreed to make regular deliveries of the claimant's cartons to a third party (Woolworth's). The defendant had made a major miscalculation of the rate. That party later threatened to stop performance until the claimant agreed a higher rate. The claimant feared that its contract with Woolworth's would be lost unless it maintained a regular and uninterrupted supply. Tucker J found that the claimant had no realistic chance to find a substitute carrier in time. This was a classic instance of the defendant having a person 'over a barrel'.⁵⁶ The

49 Also: '*The Alev*' [1989] 1 Lloyd's Rep 138, Hobhouse J; *Huyton SA v. Peter Cremer GmbH & Co.* [1999] 1 Lloyd's Rep 620, Mance J (lawful threat; commercial context); noted by D Nolan, [2000] *Restitution Law Review* 105-14; *Carillion Construction Ltd v. Felix UK Ltd* [2001] BLR 1; *Alf Vaughan & Co. v. Royscot Trust plc* [1999] 1 All ER (Comm) 856 (threat by hire-purchase company to repossess goods for non-payment is not illegitimate, because it is consistent with legal rights).

50 [1984] ICR 419, CA.

51 [1989] QB 833, Tucker J; noted by D. Fleming, [1989] CLJ 362.

52 [2008] EWHC 3205 (QB); [2008] Bus LR D55.

53 [1984] ICR 419, CA.

54 [1984] ICR 419, 428, CA, *per* Kerr LJ.

55 [1989] QB 833, Tucker J; noted by D. Fleming, [1989] CLJ 362.

56 [1989] QB 833, 838F.

claimant was entitled to withhold the promised additional payment and to recover prior overpayments.

- (3) In *Adam Opel GmbH v. Mitras Automotive UK Ltd* (2008), Deputy High Court Judge David Donaldson QC held that a renegotiation had been procured by overwhelming commercial pressure.⁵⁷ The threat by a supplier to cease to supply parts to a manufacturer of commercial vans was illegitimate and sufficiently potent. The coerced party had had no real opportunity to nullify this pressure by seeking an injunction to restrain the threatening party from acting in this manner. This case shows the courts' willingness to consider sensitively the reality of the coerced party's suggested scope for protesting and using the formal mechanism of court litigation to challenge pre-emptively the threat.⁵⁸

- 11.21 *Insufficient commercial pressure to vitiate a renegotiated agreement.* In '*The Siboen and the Sibotre*' (1976), Kerr J⁵⁹ broke new ground (in England) by suggesting that economic duress might be recognised. However, this plea failed on the present facts because the pressure was characterised as 'mere commercial pressure'.⁶⁰

The charterers of two ships fraudulently said that they faced imminent financial collapse. They told this lie to induce the owners to agree a reduction in the agreed rate of hire. The charterers knew that their statements would be highly coercive because of a recent drop in the market rate of hire (the agreed price was US\$4.40 per ton; the market rate dropped to US\$2.80 per ton). They were also aware of the owner's need to maintain the present contracts in order to meet mortgage liabilities on these vessels. Kerr J held that the fraudulent misrepresentation was the owner's primary cause of action (a finding which, it should be noted, rendered appeal from the decision on the question of economic duress highly unlikely!). Kerr J also acknowledged that economic duress should henceforth be recognised in English law, although he then held that the plea failed on this point in this case because there had been 'mere commercial pressure'.⁶¹ It is submitted that this phrase is a reference to the objective requirement that the pressure must have been so overwhelming that the coerced party had no practical alternative but to submit. However, even on this interpretation, it is not clear why the learned judge considered that the threats were objectively insufficiently coercive on these facts. But that obscurity is a matter of interpretation, an assessment of fact in this particular case. And so the doctrine of economic duress could begin to take root, watered by favourable academic comment.⁶²

- 11.22 *Duress and 'decreasing pacts'.* In *D & C Builders v. Rees* (1966), Lord Denning MR, applying the doctrine of promissory estoppel (in equity) (on decreasing pacts, see 5.45 ff; and,

57 [2008] EWHC 3205 (QB); [2008] Bus LR D55.

58 *Ibid.*, at [32] and [33].

59 [1976] 1 Lloyd's Rep 293, Kerr J; noted by J. Beatson, (1976) 92 LQR 496.

60 [1976] 1 Lloyd's Rep 293, 336.

61 [1976] 1 Lloyd's Rep 293, 336.

62 J. Beatson, (1976) 92 LQR 496, 498–9.

on this case, see 5.51), held that a promise to accept a smaller payment, *in discharge of the full debt*, could be binding. But Lord Denning further noted that equitable relief will be withheld if, on the relevant facts, equity's applicant (here the debtor, invoking the doctrine as a defence) does not 'come with clean hands'.⁶³ And so Lord Denning concluded that she could not take advantage of the doctrine of promissory estoppel in the present case because of her shabby behaviour: for she had coerced the cash-strapped builder into accepting a cheque for part-payment as full discharge.

3. UNDUE INFLUENCE⁶⁴

11.23 Nature of 'actual undue influence'. Gifts or contracts can be set aside for undue influence (on rescission, see 9.18 ff). The modern law is substantially restated in the long speeches of the House of Lords in the *Etridge* case⁶⁵ (summarised by Lewison J in *Thompson v. Foy* (2009)).⁶⁶ Undue influence can, *but need not*, involve coercion.⁶⁷ As Lord Nicholls said in the *Etridge* case (2002): (1) it 'comprises overt acts of improper pressure or coercion such as unlawful threats'⁶⁸ but (2) it has a broader 'connotation of impropriety',⁶⁹ and this can take the form of 'overt acts of persuasion'.⁷⁰ Thus, actual undue influence can cover a range of improper conduct, including coercion, misleading statements, half-truths, cunning persuasion, artful steps and guile. Lewison J in *Thompson v. Foy* (2009) referred to 'acts of overt persuasion, emotional blackmail or bullying'.⁷¹

Slade LJ in *BCCI v. Aboody* said that the four requirements of a plea of actual undue influence are: '(a) the other party to the transaction (or someone who induced the transaction for his own benefit) had the capacity to influence the complainant; (b) the influence was exercised; (c) its exercise was undue; (d) its exercise brought about the transaction.'⁷²

63 *D & C Builders v. Rees* [1966] 2 QB 617, 625, CA.

64 R. Bigwood, *Exploitative Contracts* (Oxford, 2003); P. Birks and N. Y. Chin, 'On the Nature of Undue Influence', in J. Beatson and D. Friedmann (eds.), *Good Faith and Fault in Contract Law* (Oxford, 1995), 57, especially at 57–60, 63–5, 85–8, 92–7; A. Burrows, *The Law of Restitution* (2nd edn, London, 2002), chapter 6; D. Capper, (1998) 114 LQR 479; M. Chen-Wishart, 'Undue Influence: Beyond Impaired Consent and Wrongdoing Towards a Relational Analysis', in A. Burrows and A. Rodger (eds.), *Mapping the Law: Essays in Memory of Peter Birks* (Oxford, 2006); M. Chen-Wishart, [2006] CLP 231; N. Enonchong, *Duress, Undue Influence and Unconscionable Dealing* (London, 2006); R. Goff and G. H. Jones, *The Law of Restitution* (7th edn, London, 2007), chapter 11; G. Virgo, *Principles of the Law of Restitution* (2nd edn, Oxford, 2006), chapter 10; L. McMurry, [2000] Conv 573; A. Phang and H. Tjio, [2002] LMCLQ 231; D. O'Sullivan, (2002) 118 LQR 337–51.

65 *Royal Bank of Scotland plc v. Etridge (No. 2)* [2002] 2 AC 773, HL, at [8] (generally on undue influence, see Lord Nicholls at [6] to [89], and Lord Scott at [139] to [192]); noted by M. Oldham, [2002] CLJ 29–32 and D. O'Sullivan, (2002) 118 LQR 337–51.

66 [2009] EWHC 1076 (Ch); [2010] 1 P & CR 16, at [99], Lewison J (the passage is too long to quote here); and see his supplementary observations at [100] and [101].

67 Coercion is the historical focus of the *probate* doctrine of undue influence: see P. Winder, (1939) 3 MLR 97, 104 ff.

68 *Royal Bank of Scotland plc v. Etridge (No. 2)* [2002] 2 AC 773, HL, at [8] (generally on undue influence, see Lord Nicholls at [6] to [89], and Lord Scott at [139] to [192]); noted by M. Oldham, [2002] CLJ 29–32 and D. O'Sullivan, (2002) 118 LQR 337–51.

69 *Royal Bank of Scotland plc v. Etridge (No. 2)* [2002] 2 AC 773, HL, at [32].

70 *Ibid.*, at [7] and [9].

71 [2009] EWHC 1076 (Ch); [2010] 1 P & CR 16, at [112].

72 [1990] 1 QB 923, 967.

Element (a) does not appear to add helpfully to the analysis. Elements (b) and (d) are satisfactory, although element (c) is not entirely clear. Once ‘actual undue influence’ is proved on the balance of probabilities, the claimant need not go further and show that the gift or transaction ‘calls for explanation’, that is, there is no further need to show that it is objectively extravagant or, in the case of a transaction, that it is conspicuously unbalanced.⁷³ In this sense, as Lord Browne-Wilkinson said in the *Pitt* case (1994), a victim of actual undue influence is entitled to have the transaction rescinded ‘as of right’.⁷⁴

The traditional view is that undue influence is equity’s response to improper conduct, that is, to use the jargon of modern academic analysis, that it is ‘defendant-sided’. In *R v. Her Majesty’s Attorney-General for England and Wales* (2003), Lord Hoffmann said in the Privy Council: ‘Undue influence has concentrated in particular upon the unfair exploitation by one party of a relationship which gives him ascendancy or influence over the other.’⁷⁵ Similarly, Lord Hobhouse said in the *Etridge* case (2002) that undue influence is an ‘equitable wrong committed by the dominant party against the other which makes it unconscionable for the dominant party to enforce his legal rights against the other’.⁷⁶ According to this view, it is insufficient that the claimant has suffered from some form of transactional disadvantage or bargaining handicap.

The view that rescission for undue influence is equity’s response to improper conduct was opposed by Birks and Chin in 1995.⁷⁷ In their opinion, the true view is that undue influence is ‘plaintiff-sided’ because its essence is ‘impairment of the capacity of the plaintiff to make the decision which is impugned’;⁷⁸ ‘the plaintiff ... has, to a sufficiently extreme degree, a sub-standard judgemental capacity, and the source of the impairment is the character of the relationship in which he finds himself.’⁷⁹ Birks and Chin’s approach comes close to creating a new jurisdiction of ‘incapacity’, beyond the established situations of mental infirmity, and infancy (on these, see 1.09 at (4)). However, in general, Birks and Chin’s argument is not accepted.⁸⁰ Thus, Bigwood has re-emphasised the orthodox view that undue influence is an abuse of a relationship, sometimes involving coercion, but sometimes extending to subtler forms of influence.⁸¹ Capper (2010) has also opposed the Birks and Chin argument as ‘contrary to the basic principle that a contracting party should not be deprived of bargained-for advantage unless the bargaining process fell short of

73 *Ibid.*, at [12] and [156].

74 *CIBC Mortgages plc v. Pitt* [1994] 1 AC 200, 209B–C, HL.

75 [2003] UKPC 22; [2003] EMLR 24, at [21].

76 *Royal Bank of Scotland plc v. Etridge (No. 2)* [2002] 2 AC 773, HL, at [103].

77 P. Birks and N. Y. Chin, ‘On the Nature of Undue Influence’, in J. Beatson and D. Friedmann (eds.), *Good Faith and Fault in Contract Law* (Oxford, 1995), 57–97.

78 *Ibid.*, at 59.

79 *Ibid.*, at 89.

80 Unless the following isolated remark of Mummery LJ is taken as implicit support, in *Pesticcio v. Huet* [2004] EWCA Civ 372; [2004] NPC 55, at [20]: ‘A transaction may be set aside by the court, even though the actions and conduct of the person who benefits from it could not be criticised as wrongful.’ Christopher Clarke J in *Birmingham City Council v. Forde* [2009] EWHC 12 (QB); [2010] 1 All ER 802, at [103], citing this case, said that undue influence does not require ‘any wrongful or dishonest act’.

81 R. Bigwood, *Exploitative Contracts* (Oxford, 2003), 467 ff; and R. Bigwood, (1995) 16 OJLS 503; Bigwood’s criticism was in turn described by P. Birks, [1997] *Restitution Law Review* 72, 76 n. 20, as ‘not wholly convincing’; and see P. Birks, (2004) 120 LQR 34–7 (reiteration of his ‘claimant-sided theory’ by reference to *Hammond v. Osborn* [2002] EWCA Civ 885; [2002] WTLR 1125: on this last case, see the text below).

societal standards of freeness and fairness.’⁸² Outright wicked, cynical or conscious exploitation is not required. The defendant might have acted in some cases in a morally upright and even righteous way (see the next case), but he or she will nevertheless be castigated in equity for not having taken proper steps to ensure that the transaction or gift was the true product of the other party’s free consent, and that the latter was insulated from the relevant influence. For example, in the seminal case of *Allcard v. Skinner* (1887), where a novice in a nunnery had handed over all her property to the convent, Lindley LJ said:⁸³

I believe that in this case there was in fact no unfair or undue influence brought to bear on the plaintiff other than such as inevitably resulted from the training she had received, the promise she had made, the vows she had taken, and the rules to which she submitted herself. But her gifts were in fact made under a pressure which, whilst it lasted, the plaintiff could not resist.

And Sir Eric Sachs in *Lloyds Bank v. Bundy* (1975) said:

[O]nce the existence of a special relationship has been established, then any possible use of the relevant influence is, irrespective of the intentions of the persons possessing it, regarded in relation to the transaction under consideration as an abuse – unless and until the duty of fiduciary care has been shown to be fulfilled.⁸⁴

Allcard v. Skinner, just examined, shows that equity’s paternalistic protection against abuse of the truly weak and vulnerable parties to lopsided relationships is so intense that there is no need to colour a set of facts as an example of morally reprehensible misconduct by the stronger party: instead, it is enough that the stronger party has not discharged the obligation, arising from the unequal nature of the relationship, to ensure that the weaker party is enabled, by resort to outside advice, to make a clear and free evaluation of the merits of the proposed transaction or transfer.

In *Drew v. Daniel* (2005), an elderly aunt was bullied by a forceful nephew into making a deed of resignation from a family trust.⁸⁵ She had been (metaphorically) ‘pushed around’. The judge was satisfied that she had succeeded in establishing actual undue influence. The appeal against that decision failed. Ward LJ said:

[I]n the case of actual undue influence something has to be done to twist the mind of a donor [or contracting party] whereas in cases of presumed undue influence it is more a case of what has not been done namely ensuring that independent advice is available to the donor.

In many cases, the stronger party’s conduct can readily be coloured as morally reprehensible, not because this is necessary as a matter of law, but in order to substantiate the court’s sense that there has been a failure to insulate the weaker party from the danger

82 D. Capper, (2010) 126 LQR 403, 418.

83 (1887) 36 Ch D 145, 185, CA.

84 [1975] QB 326, 343, CA.

85 [2005] EWCA Civ 507; [2005] 2 P & CR 14, at [31], [32] and [36].

of improper influence. Thus, Lord Nicholls said in the *Etridge* case (2002):⁸⁶ 'Undue influence has a connotation of impropriety. In the eye of the law, undue influence means that influence has been misused.' And, in a later passage, he said:⁸⁷

Proof that the complainant placed trust and confidence in the other party in relation to the management of the complainant's financial affairs, coupled with a transaction which calls for explanation, will normally be sufficient, failing satisfactory evidence to the contrary, to discharge the [complainant's] burden of proof ... [P]roof of these two facts is *prima facie* evidence that the defendant abused the influence he acquired in the parties' relationship. He preferred his own interests. He did not behave fairly to the other. So the evidential burden then shifts to him. It is for him to produce evidence to counter the inference which otherwise should be drawn.

Birks remained committed to the 'plaintiff-sided' theory of undue influence. This led him to interpret cases through this unorthodox prism. So, for example, Birks⁸⁸ presented a highly sanitised version of the donee, Mrs Osborn's, conduct in *Hammond v. Osborn* (2002),⁸⁹ although that case is in fact, in one judge's opinion, a clear example of 'sinister' manipulation (see the summary below).

In Hammond v. Osborn (2002), a frail and sick man, having received modest assistance from a stranger, transferred very large gifts to her as a gift. The Court of Appeal's judgment boils down to this: even though he knew what he was doing, he was not in full control of his decision-making powers, having become unduly attached to the donee in a prolonged state of sentimental affection; furthermore, the donee knew this, but failed to ensure that 'fair play' was maintained in their dealings. The donor had been the donee's prey.

By contrast, Birks' interpretation of the 'core' problem in that case accentuates the donor's lack of clear-mindedness. This fails to reflect the censorious observation of Nourse LJ, one of the appeal judges, who said that the donee's 'conduct' was clearly not 'unimpeachable'; indeed, it had a 'sinister appearance'. Similarly, Ward LJ said that she had not displayed 'fair play'.⁹⁰ This is the traditional perspective of 'defendant-sided' impropriety. Indeed, the opportunity for improper influence had been conceded by the defendant's counsel; then the defendant failed to satisfy the court that the vulnerable party (now deceased) had been emancipated from that influence. In this sense, the defendant had taken improper advantage of the vulnerability of the other party within this relationship.

In short, 'defendant-sided' impropriety is the core of undue influence, and Birks and Chin are wrong to suggest that equity is responsive to improper conduct only within the doctrine of 'unconscionability' (on which see 11.36).

86 *Royal Bank of Scotland plc v. Etridge* (No. 2) [2002] 2 AC 773, HL, at [32].

87 *Ibid.*, at [103].

88 P. Birks, 'Undue Influence as Wrongful Exploitation' (2004) 120 LQR 34–7; see also P. Birks, *Unjust Enrichment* (Oxford, 2005), 176–8.

89 [2002] EWCA Civ 885; [2002] WTLR 1125, at [31].

90 *Ibid.*, at [61].

11.24 As mentioned at 11.23, actual undue influence is not equity's counterpart to common law duress. Instead, coercion⁹¹ is one of several possible modes of 'actual undue influence'. The courts have consistently noted the wide and pliable nature of undue influence.

Lord Scarman in *National Westminster Bank plc v. Morgan* (1985) said that there are no⁹² 'precisely defined ... limits to the equitable jurisdiction of a court to relieve against undue influence ... A court in the exercise of this ... is a court of conscience. Definition is a poor instrument when used to determine whether a transaction is [to be impeached on this basis].'

Lord Clyde said in the *Etridge* case (2002):⁹³ 'It is something which can be more easily recognised when found than exhaustively analysed in the abstract.' And, in the same case, Lord Hobhouse said:⁹⁴

[Undue influence is an] equitable wrong committed by the dominant party against the other which makes it unconscionable for the dominant party to enforce his legal rights against the other. It is typically some express conduct overbearing the other party's will. It is capable of including conduct which might give a defence at law, for example, duress and misrepresentation. Indeed many of the cases relating to wives who have given guarantees and charges for their husband's debts involve allegations of misrepresentation. (*O'Brien*⁹⁵ was such a case.) Actual undue influence does not depend upon some pre-existing relationship between the two parties though it is most commonly associated with and derives from such a relationship. He who alleges actual undue influence must prove it'

Lindley LJ in *Allcard v. Skinner* (1887) (the case concerning the gift of all her worldly goods by a novice to a convent) said:⁹⁶

To protect people from being forced, tricked or misled in any way by others into parting with their property is one of the most legitimate objects of all laws; and ... undue influence has ... been developed by the necessity of grappling with insidious forms of spiritual tyranny and with the infinite varieties of fraud. As no Court has ever attempted to define fraud so no Court has ever attempted to define undue influence, which includes one of its many varieties. The undue influence which Courts of Equity endeavour to defeat is the undue influence of one person over another ... [The] influence of one mind over another is very subtle, and of all influences religious influence is the most dangerous and the most powerful, and to counteract it Courts of Equity have gone very far.

Lord Denning MR in *Lloyds Bank Ltd v. Bundy* (1975) referred to actual undue influence as involving 'some fraud or wrongful act'.⁹⁷ Similarly, Lord Browne-Wilkinson in the

91 Coercion is the historical focus of the *probate* doctrine of undue influence: P. Winder, (1939) 3 MLR 97, 104 ff.

92 [1985] AC 686, 709, HL; noted by N. Andrews, [1985] CLJ 192.

93 *Royal Bank of Scotland plc v. Etridge* (No. 2) [2002] 2 AC 773, HL, at [92].

94 *Ibid.*, at [103].

95 In accordance with Lord Browne-Wilkinson's exposition in *Barclays Bank plc v. O'Brien* [1994] 1 AC 180, 189–90, HL.

96 *Allcard v. Skinner* (1887) 36 Ch D 145, 183, CA.

97 [1975] QB 326, 338A, CA.

Pitt case (1994) referred to actual undue influence as a ‘species of equitable fraud’.⁹⁸ This notion has become rather opaque. But it should be noted that equitable ‘fraud’ is not to be confused with the relatively precise and narrow notion of ‘deceit’ at common law, and the doctrine of fraudulent misrepresentation.

11.25 ‘*Presumed undue influence*’. In the absence of proven ‘actual undue influence’, the complainant must show:

- (1) the existence of such a relationship of trust and confidence based on either (a) standard recognition of the parties’ roles, for example, the inequality between solicitor and client or doctor and patient, or (b) *ad hoc* recognition, based on the particular nature of the parties’ relationship, for example, one friend enjoying much greater influence over the other (see 11.26 for more on this first category);
- (2) that the transaction ‘calls for explanation’ (that is, it is substantively one-sided and suspicious) (the ‘ace card’) (see 11.26 for more on this second category);
- (3) whereupon *it is incumbent on the superior party to retrieve the position* and demonstrate that the inferior party had entered the transaction ‘with her eyes open’, exercising a free and informed consent (see 11.27 for more on this third category).

11.26 *Presumed categories*. The House of Lords in the *Etridge* case (2002)⁹⁹ noted that it had become customary to distinguish within the broad category of ‘presumed undue influence’ cases (‘Class 2’ situations) between:¹⁰⁰

- (a) those (‘Class 2A’) which are standard instances of legally recognised protected relationships; and
- (b) those (‘Class 2B’) which are shown on the facts of a particular case to disclose a relationship of trust, confidence, dependence, loyalty, etc.

The main examples of relationships within Class 2A, that is, instances of plain inequality between the parties, are: trustee and beneficiary; spiritual advisor (or priest) and devotee;¹⁰¹ parent and child; guardian and ward; and solicitor and client¹⁰² (even if they are cohabiting).¹⁰³ As Lord Nicholas in the *Etridge* case said, considering Class 2A, ‘[t]he law

98 *CIBC Mortgages plc v. Pitt* [1994] 1 AC 200, 209B, HL.

99 *Royal Bank of Scotland plc v. Etridge (No. 2)* [2002] 2 AC 773, HL, at [8] (generally on undue influence, see Lord Nicholls at [6] to [89], and Lord Scott at [139] to [192]); noted by M. Oldham, [2002] CLJ 29–32 and D. O’Sullivan, (2002) 118 LQR 337–51.

100 In accordance with Lord Browne-Wilkinson’s exposition in *Barclays Bank plc v. O’Brien* [1994] 1 AC 180, 189–90, HL.

101 *Allcard v. Skinner* (1887) 36 Ch D 145, CA (nun making large gifts to the head of the nunnery; but the nun was too slow in seeking rescission on the facts); and *Morley v. Loughman* [1893] 1 Ch 736, 756, Wright J (where the exertion of ascendancy over a religious convert was proved by clear ‘inferences’; no need to rely on any presumption).

102 For parent/child, guardian/ward, and solicitor/client, see the authorities cited in *Chitty on Contracts* (30th edn, London, 2008), 7-074 ff.

103 *Markham v. Karsten* [2007] EWHC 1509 (Ch), at [35] and [36], *per* Briggs J.

has long recognised the need to prevent abuse of influence in these “relationship” cases despite the absence of evidence of overt acts of persuasive conduct.¹⁰⁴ Here, the irrebuttable presumption is that the ‘stronger’ party had influence over the other.¹⁰⁵ However, as Lords Nicholls and Hobhouse noted in the *Etridge* case (2002), within both Class 2A and Class 2B, there is *no presumption* that the dominant party has in fact abused his relationship.¹⁰⁶ Something more must be added: only if the gift is substantial, or the transaction ‘calls for explanation’, will the dominant party need to show that in fact the weaker party was not the victim of undue influence. The *Etridge* case (2002) discarded the test of ‘manifest disadvantage’ and substituted the test that the gift or transaction should ‘call for explanation’ or that it should be not ‘readily explicable’¹⁰⁷ (the ‘calls for explanation’ requirement has now been considered in numerous cases).¹⁰⁸ Lord Nicholls said in the *Etridge* case (2002):¹⁰⁹

Proof that the complainant placed trust and confidence in the other party in relation to the management of the complainant’s financial affairs, coupled with a transaction which calls for explanation, will normally be sufficient, failing satisfactory evidence to the contrary, to discharge the burden of proof ... On proof of these two matters the stage is set for the court to infer that, in the absence of a satisfactory explanation, the transaction can only have been procured by undue influence. So the evidential burden shifts to [the defendant]. It is for him to produce evidence to counter the inference which otherwise should be drawn.¹¹⁰

Lord Nicholls said that ordinarily a spouse’s decision to act as surety for the other spouse’s debts can be attributed to readily explicable motives.¹¹¹ This situation does not, therefore, ordinarily ‘call for explanation’. However, perhaps a guarantee offered in the following situation will ‘call for explanation’. X Bank lends £1m to Brian, supported by a charge over his property. The loan is repayable in twelve months’ time. After six months, however, the bank becomes concerned that Brian might default and that his property’s value has diminished. An arrangement is made to procure further security and a guarantee from Brian’s wife, Cynthia. In this situation, it is arguable that Cynthia’s provision of a guarantee and security ‘calls for explanation’ because the borrower has gained nothing new, and the lender is wholly benefited by Cynthia’s intervention. (This situation mirrors the second guarantee and provision of security provided by Bundy on behalf of his son’s loan in *Lloyds Bank v. Bundy* (1975): see 11.30).¹¹²

104 *Royal Bank of Scotland plc v. Etridge (No. 2)* [2002] 2 AC 773, HL, at [10].

105 *Ibid.*, at [18].

106 *Ibid.*, at [14] and [18], *per* Lord Nicholls, and at [104], *per* Lord Hobhouse.

107 *Royal Bank of Scotland plc v. Etridge (No. 2)* [2002] 2 AC 773, HL, at [21] to [31], *per* Lord Nicholls.

108 E.g. *Macklin v. Dowsett* [2004] EWCA Civ 904; [2004] 2 EGLR 75; [2004] 34 EG 68; [2005] WTLR 1561, at [30] ff, *per* Auld LJ; *Turkey v. Awadh* [2005] EWCA Civ 382; [2005] 2 P & CR 29, at [15], and [20] ff, *per* Buxton LJ; *Thompson v. Foy* [2009] EWHC 1076 (Ch); [2010] 1 P & CR 16, at [100] and [108], *per* Lewison J.

109 *Royal Bank of Scotland plc v. Etridge (No. 2)* [2002] 2 AC 773, HL, at [14].

110 *Ibid.*, *per* Lord Hobhouse at [107] and Lord Scott at [153].

111 *Ibid.*, at [30] and [31], *per* Lord Nicholls.

112 [1975] QB 326, CA.

- 11.27 If the transaction does indeed ‘call for explanation’, it becomes necessary for the stronger party to produce evidence to convince the court that the weaker party’s consent was freely and advisedly given,¹¹³ without any improper influence being exerted. The obtaining of independent legal advice can, but not necessarily will, demonstrate that the weaker party did freely consent. As Mummery LJ said in *Pesticcio v. Huet* (2004):¹¹⁴

The participation of a solicitor is not, however, a precaution which is guaranteed to work in every case. It is necessary for the court to be satisfied that the advice and explanation by, for example, a solicitor, was relevant and effective to free the donor from the impairment of the influence on his free will and to give him the necessary independence of judgment and freedom to make choices with a full appreciation of what he was doing.

In *Randall v. Randall* (2004),¹¹⁵ the judge summarised the law as follows:

Independent advice is a factor, and an important factor, for the court to take into account when weighing all the evidence. However, the weight, or importance, to be attributed to such advice depends on all the circumstances. The circumstances in which the advice is given, or the quality of that advice, may not be sufficient to bring home to a complainant a proper understanding of what he is about to do. And even if a person understands fully the implications of the proposed transaction, yet the complainant may still remain under the undue influence of another. Proof of outside advice does not, of itself, necessarily show that the subsequent completion of the transaction was free from the exercise of undue influence. It is a question of fact whether the outside advice had the appropriate ‘emancipating’ effect, and that question of fact has to be decided having regard to all the evidence in the case.

- 11.28 *Relationship of trust and confidence arising during protracted stages of a transaction.* Normally, the relevant relationship will antedate the transaction which is now challenged. But, in *Macklin v. Dowsett* (2004), the Court of Appeal held that such a relationship had arisen during protracted property dealings between the parties, even though there had been no relationship of trust and confidence between them before those dealings had commenced.¹¹⁶ It was enough that a relationship of ascendancy and dependence had emerged during the parties’ dealings. Those dealings culminated in the arrangement which was now successfully impugned: Dowsett’s grant to Macklin of an option to ‘buy out’ Dowsett’s lifetime rent-free tenancy for a mere £5,000 if Dowsett did not succeed himself in developing the land within the tight ‘window’ of the terms of a planning permission. The court held that Macklin could not take advantage of that option. It had been obtained as a result of undue influence.

113 *Birmingham City Council v. Forde* [2009] EWHC 12 (QB); [2010] 1 All ER 802, at [105], *per* Christopher Clarke J: ‘[T]he problem is not lack of understanding but lack of independence.’

114 [2004] EWCA Civ 372; [2004] NPC 55, at [23].

115 [2004] EWHC 2258 (Ch); [2005] 1 P & CR DG4, at [38] (a decision of Edward Bartley Jones QC, in the Chancery Division).

116 [2004] EWCA Civ 904; [2004] 2 EGLR 75; [2004] 34 EG 68; [2005] WTLR 1561.

- 11.29 *Duty not to suppress a material factor.* The Court of Appeal in *Hewett v. First Plus Financial Group* (2010)¹¹⁷ held that, *once a relationship of trust and confidence is shown to exist* between husband and wife, this relationship can import a duty to refrain from deliberate suppression of a material fact. In this case, the suppressed fact was that the husband was having an affair with another woman. Had the wife known this, it is possible – and perhaps likely – that she would not have proceeded with the refinancing of the husband's debts by agreeing to provide security for a loan made by the claimant finance company to her husband. Part of the security for that loan was her share of the matrimonial home. The Court of Appeal held that the lender had constructive notice of the fact that the wife had been the victim of a material non-disclosure (the lender had failed to insist that the wife should obtain independent legal advice before assenting to the new financing arrangement, and to her provision of security). For this reason, the lender could not enforce its security against her (although the security provided by the husband in his own name was open to enforcement by the lender, because the husband had defaulted on the loan).
- 11.30 *Banker and customer.* Because the banker/customer relationship is not in the (hallowed) list of recognised relationships of dependence, *it is a question of fact* whether a particular bank's customer has in fact placed such trust and confidence in a bank's staff or officials. In *Lloyds Bank v. Bundy* (1975)¹¹⁸ (examined below), the bank had assumed such a special relationship, whereas, in *National Westminster Bank plc v. Morgan* (1985), the House of Lords held that Mrs Morgan's dealings with her bank 'never went beyond the normal business relationship of banker and customer'.¹¹⁹ In *Lloyds Bank v. Bundy* (1975),¹²⁰ a majority of the Court of Appeal, applying orthodox principles of undue influence, held on the facts of the case that the bank had 'crossed the line'. As a result, it had assumed a special relationship of trust and confidence towards their customer, 'old' Mr Bundy, who had guaranteed his only son's business debts with the bank. The court held that there had been a consequent duty to ensure that he did not enter into an especially onerous guarantee of his son's business debts without first having obtained independent legal advice. In the absence of this, the guarantee could be set aside because it was vitiated by undue influence.

In Lloyds Bank Ltd v. Bundy (1975), over many years, the Bundys had formed a relatively close relationship with the officials of the bank's Salisbury branch. 'Old' Mr Bundy had already agreed one guarantee of his son's debts. The guarantee was supported by a charge, in favour of the bank, against his property, 'Yew Tree Farm'. Before assenting to this first guarantee, he had obtained independent advice. The fateful transaction involved a further secured guarantee

117 *Hewett v. First Plus Financial Group* [2010] EWCA Civ 312; [2010] Fam Law 589, adopting David Richards J's statement in *Royal Bank of Scotland v. Chandra* [2010] EWHC 105 (Ch): '[D]eliberate suppression of information because the husband knows that, if disclosed, it will deter the wife from giving the guarantee, will involve an abuse by him of her confidence. It would be unconscionable and rightly categorised as unacceptable means.'

118 [1975] QB 326, CA.

119 [1985] AC 686, 702G, HL; noted by N. Andrews, [1985] CLJ 192.

120 [1975] QB 326, CA.

given by the father of the same debts owed by his son to the bank. This new transaction was advantageous to the bank: for it gave the bank additional security and a reduction in the level of the son's borrowing limit. On this occasion, the bank had been represented by a new man (Mr Head). Old Mr Bundy signed without obtaining fresh independent legal advice. The bank did not perceive the need to impress upon him the merits of obtaining such advice. Later, the bank sought to invoke its security against the guarantor. The Court of Appeal held by a majority (Cairns and Sachs LJ) that orthodox principles of undue influence justified rescission of the second guarantee.

The Court of Appeal held that this guarantee was vitiated by undue influence. The bank had assumed on these special facts a position of trust and confidence, because of the regularity and closeness of the dealings between the bank and Bundy senior. The bank had not done enough to recommend that Bundy senior should shield himself from the peril that he might be lured into acting most imprudently to protect his son and to heed the advice of the bank. In short, the bank was seriously 'conflicted' on these facts. As for the second guarantee, Sachs LJ explained that:¹²¹

The situation was ... one which to any reasonably sensible person ... cried aloud for Mr Bundy's need for careful independent advice. The bank's failure on these facts to advise that he should receive such advice was a breach of a fiduciary¹²² duty, arising from its position towards Bundy of trust and confidence. In those circumstances, it would be contrary to public policy [for the] benefit of the transaction to be retained by the [bank].¹²³

It will be seen that here undue influence operates to impose a positive duty to act. This is not the same as inferring that there have been 'overt acts of coercion or persuasion' (see also the comments at 11.24 above).

In *R v. Her Majesty's Attorney-General for England and Wales* (2003),¹²⁴ a soldier had signed a confidentiality clause as a condition of remaining with the elite SAS regiment. He later challenged the validity of that agreement on the basis that it resulted from duress or undue influence. The Privy Council unanimously rejected the duress (11.10) plea, and, by a majority (Lord Scott dissenting), the undue influence plea. As for the latter, the Privy Council held that, even assuming that the Crown occupied a position of superiority on these facts, there had been no exploitation of his position, nor had there been any objectionable failure to ensure that he should receive independent legal advice.¹²⁵ Lord Scott dissented on this last point.¹²⁶ In his view, this was a 'classic' situation of domination amounting to undue influence, where the Crown should have insisted that a lifetime confidentiality obligation should only be undertaken if an employee has received independent legal advice.

¹²¹ *Ibid.*, at 345.

¹²² *Calvert v. William Hill Credit Ltd* [2008] EWCA Civ 1427; [2009] Ch 330, at [53]; *Parker and Mellows: The Modern Law of Trusts* (9th edn, London, 2008), 10-048 ff; J. Edelman, 'When Do Fiduciary Duties Arise?' (2010) 126 LQR 302.

¹²³ [1975] QB 326, 346, CA.

¹²⁴ [2003] UKPC 22; [2003] EMLR 24.

¹²⁵ *Ibid.*, at [24] to [28].

¹²⁶ [2003] UKPC 22; [2003] EMLR 24, at [45].

Lord Scott's analysis is analogous to the decision of the majority in *Lloyds Bank v. Bundy*, examined above.

The task of showing a relationship of dependence has become harder because of changes in most ordinary banking relationships. Compared with the 1970s, nowadays many people never meet their 'bank manager', even assuming that such an official has been nominated to deal with the relevant customer. In these modern conditions of faceless, telephonic banking, often conducted on the telephone with a call-centre operative who might be sitting in Edinburgh or Mumbai, there are many more people in the position of Mrs Morgan in *National Westminster Bank plc v. Morgan* (1985),¹²⁷ rather than the one-to-one 'special banking relationship' identified by the Court of Appeal in *Lloyds Bank v. Bundy* (1975).¹²⁸ But, even if a customer shows that he did have a relationship of trust and dependence with a bank, the Privy Council's decision in *National Commercial Bank (Jamaica) Ltd v. Hew* (2003)¹²⁹ shows that he must also demonstrate that the relevant transaction was disadvantageous, that is, it was conspicuously favourable to the bank. Without this, Lord Millett explained that there will be no reason for the court to conclude that the bank has abused the relationship. For this reason, the bank's customer in the *Hew* case failed to impugn a straightforward loan earmarked by the lender only for use in a nominated commercial project. The fact that this project misfired was irrelevant. The bank had not behaved improperly.¹³⁰

11.31 *Lenders, guarantors and third parties' wrongdoing.*¹³¹ The House of Lords in the *Etridge* case (2002),¹³² now the leading case, reviewed its earlier decisions in *Barclays Bank v. O'Brien* (1994)¹³³ and *CIBC v. Pitt* (1994).¹³⁴ This line of cases concerns a lender's possible actual or 'constructive' awareness (deemed knowledge) that a guarantor of a loan has been the victim of the borrower's misrepresentation, coercion or undue influence. This tripartite relationship involves the following elements:

- (1) A and X are a married couple or A and X have a sexual, emotional or other non-commercial relationship;

127 [1985] AC 686, HL; noted by N. Andrews, [1985] CLJ 192.

128 [1975] QB 326, CA.

129 [2003] UKPC 51.

130 *Ibid.*, at [35].

131 N. Enonchong, *Duress, Undue Influence and Unconscionable Dealing* (2006), Part IV; D. O'Sullivan, S. Elliott and R. Zakrzewski, *The Law of Rescission* (Oxford, 2008), chapter 9.

132 *Royal Bank of Scotland plc v. Etridge (No. 2)* [2002] 2 AC 773, HL, at [48], *per* Lord Nicholls: adopted also in both Canada (M. H. Ogilvie, 'The Reception of Etridge (No. 2) in Canada' [2008] JBL 191) and New Zealand (D. Capper, 'The Unconscionable Bargain in the Common Law World' (2010) 126 LQR 403, 413 n. 84), but Australia has adhered to its special equity for surety wives (*ibid.*, at 411, noting *Garcia v. National Australia Bank Ltd* (1998) 194 CLR 395 (High Court of Australia) (applying *Yerkey v. Jones* (1939) 63 CLR 649, High Court of Australia)); R. Bigwood, 'From Morgan to Etridge: Tracing the (Dis)Integration of Undue Influence ...', in J. W. Neyers, R. Bronaugh and S. G. A. Pitel (eds.), *Exploring Contract Law* (Oxford, 2009), 379 ff.

133 [1994] 1 AC 180, HL.

134 [1994] 1 AC 200, HL.

- (2) X wishes to receive (or in some cases to increase or simply continue) a loan from B, which is normally a bank or other commercial lender;
- (3) A ultimately agrees to act as surety for X's repayments to B, and so A assumes a direct contractual tie (under a contract of guarantee) with B;
- (4) furthermore, the guarantee is normally supported by a charge in favour of B upon A's interest in the matrimonial or quasi-matrimonial home;
- (5) when B calls upon A to honour the guarantee, normally to compel a sale of A's property in accordance with the charge in B's favour, A protests that she has been the victim of some legal wrong or impropriety committed by X, and of which B has express or constructive notice;
- (6) this wrong or impropriety might be any of the following:
 - (a) a misrepresentation by the guarantor on which the borrower relied; or
 - (b) a deliberate and material non-disclosure (as in *Hewett v. First Plus Financial Group* (2010): see 11.29);¹³⁵ or
 - (c) duress; or
 - (d) actual undue influence; or
 - (e) a presumed form of undue influence: if the guarantor wishes to show 'presumed undue influence', it will be necessary to prove both (i) a relationship of trust and confidence (that is, that the guarantor (typically the wife) habitually showed great (but not necessarily complete and unqualified)¹³⁶ deference to the other's financial decision-making); and (ii) that the guarantee 'called for explanation' (see the discussion of this requirement at 11.26).

11.32 The House of Lords in *Barclays Bank v. O'Brien* (1994)¹³⁷ and *CIBC v. Pitt* (1994)¹³⁸ noted that there are three ways in which a guarantor, A, might show that the contract of surety between her and B is voidable because of X's (the husband, etc.) wrong *vis-à-vis* A:¹³⁹

- (1) B procures A's surety agreement through X as B's 'agent' and so suffers the consequence of the latter's knowledge being 'imputed' to B; or
- (2) B has actual knowledge of some legal wrong (whether a misrepresentation, undue influence, etc.) committed by X against A, which induced A to stand as X's surety; or
- (3) constructive notice of such a wrong can be imputed to B.

The lender will be 'in the clear' if the surety entered into the guarantee after obtaining independent legal advice. But, if this requirement is not satisfied, the lender becomes

¹³⁵ *Hewett v. First Plus Financial Group* [2010] EWCA Civ 312; [2010] Fam Law 589, adopting David Richards J's statement in *Royal Bank of Scotland v. Chandra* [2010] EWHC 105 (Ch): '[D]eliberate suppression of information because the husband knows that, if disclosed, it will deter the wife from giving the guarantee, will involve an abuse by him of her confidence. It would be unconscionable and rightly categorised as unacceptable means.'

¹³⁶ *Hewett v. First Plus Financial Group* [2010] EWCA Civ 312; [2010] Fam Law 589.

¹³⁷ [1994] 1 AC 180, HL.

¹³⁸ [1994] 1 AC 200, HL.

¹³⁹ *Barclays Bank plc v. O'Brien* [1994] 1 AC 180, HL; *CIBC Mortgages plc v. Pitt* [1994] 1 AC 200, HL.

vulnerable, on the basis of constructive notice, if the surety was the victim of undue influence or some other legal wrong. Route (3) above will now be explained.

- 11.33 *Constructive notice.* The House of Lords in the *Etridge* case (2002)¹⁴⁰ made clear that *Barclays Bank v. O'Brien* (1994)¹⁴¹ (see the preceding paragraph) should be reconceptualised as follows. In surety transactions, the lender, normally a bank, is 'put on inquiry' because of its awareness of (a) the emotional nature of the relationship between the borrower and the guarantor and (b) the intrinsically onerous nature of a guarantee of a loan, especially if the loan is supported by a charge upon the equity within the matrimonial or cohabitants' home. As for (a), marital relations remain the commonest instances of such emotional relationships. But the House of Lords broadened the categories to include all other family, emotional and sexual relationships known to the bank. This will include the ties between father and daughter,¹⁴² or mother and son. Indeed, it covers all 'non-commercial' relationships between borrower and guarantor. However, the House of Lords in the *Etridge* case (2002),¹⁴³ following the *Pitt* case (1994),¹⁴⁴ acknowledged that a lender will not be fixed with constructive notice in the case of a joint loan, unless 'the bank is aware that the loan is being made for the husband's purposes, as distinct from their joint purposes', that is, the joint loan will be pocketed solely by the husband.
- 11.34 *Bank must ensure that guarantor obtains independent advice.* The bank should require the prospective surety to obtain independent legal advice (or a 'senior' bank official should sufficiently explain the transaction).¹⁴⁵ The *Etridge* case (2002) refines the 'cautionary' steps to be taken by the bank in this situation. The case creates a 'protocol' governing the bank's conduct in these matters. If the bank satisfies this set of guidelines, it will normally be 'in the clear'¹⁴⁶ even if there has been some impropriety committed by the borrower upon the guarantor (unless it has *actual knowledge* of some impropriety or special vulnerability).¹⁴⁷
- 11.35 *Nature of independent legal advice.* The lawyer who advises the prospective guarantor, the wife, need not be acting solely for that party: he can be acting jointly for borrower and guarantor. A lawyer instructed by the guarantor, or jointly by borrower and guarantor, for this purpose, would not be an agent for the bank.¹⁴⁸ The lawyer's advice should be thorough, in accordance with clear guidelines given by the House of Lords, effectively a second protocol, in the *Etridge* case (2002). The lawyer must explain the nature of the transaction and its effect, including the obvious risks of both the loss of the matrimonial home and of the guarantor's bankruptcy; the seriousness of these risks; the prospective

140 *Royal Bank of Scotland plc v. Etridge (No. 2)* [2002] 2 AC 773, HL.

141 *Barclays Bank plc v. O'Brien* [1994] 1 AC 180, HL.

142 *Royal Bank of Scotland plc v. Etridge (No. 2)* [2002] 2 AC 773, HL, at [84].

143 *Ibid.*, at [48], *per* Lord Nicholls.

144 *CIBC Mortgages plc v. Pitt* [1994] 1 AC 200, HL.

145 *Ibid.*, at [191] proposition (5).

146 *Ibid.*, at [79] proposition (3) and [191] proposition (4).

147 *Ibid.*, at [191] proposition (6).

148 *Ibid.*, at [77] and [78].

guarantor's capacity to walk away from these risks by electing not to sign; and the scope for further negotiation.¹⁴⁹ This is an exacting duty. The lawyer should refrain from 'rubber-stamping'.¹⁵⁰ The solicitor's task is not confined to enabling the prospective surety to understand the transaction; he must go further and act as a buffer between the lender and any source of undue influence (the borrower, probably waiting outside the bank in the car, while the guarantor attends to the paperwork).¹⁵¹

4. UNCONSCIONABILITY OR EXPLOITATION¹⁵²

- 11.36 Contracts can be set aside for unconscionability (on rescission, see 9.18 ff). At the core of this equitable doctrine is the notion of conscious and reprehensible exploitation of a position of acute vulnerability: however, there is no need for coercion (compare the doctrine of duress, explained at 11.02); nor is it necessary to show that overt acts of persuasion have been used (compare the doctrine of actual undue influence, explained at 11.23); nor is there need for a relationship of trust and confidence to have antedated the occasion when exploitation occurred (compare the doctrine of presumed undue influence, explained at 11.25). In *Alec Lobb (Garages) Ltd v. Total Oil GB Ltd* (1983), Peter Millett QC (later Lord Millett, and one of the greatest authorities in the twentieth century on equity) offered this definition of the modern doctrine of unconscionability:¹⁵³

[T]here must be some impropriety, both in the conduct of the stronger party and in the terms of the transaction itself (though the former may often be inferred from the latter in the absence of an innocent explanation) which in the traditional phrase 'shocks the conscience of the court', and makes it against equity and conscience of the stronger party to retain the benefit of the transaction he has unfairly obtained.

Similarly, Browne-Wilkinson J said in *Multiservice Bookbinding Ltd v. Marden* (1979) that equity intervenes here only if 'one of the parties to [the transaction] has imposed the objectionable terms in a morally reprehensible manner, that is to say, in a way which affects his conscience'.¹⁵⁴

149 *Ibid.*, at [65].

150 *Ibid.*, at [115].

151 *Ibid.*, at [111].

152 N. Bamforth, [1995] LMCLQ 538; R. Bigwood, *Exploitative Contracts* (Oxford, 2003); P. Birks and N. Y. Chin, 'On the Nature of Undue Influence', in J. Beatson and D. Friedmann (eds.), *Good Faith and Fault in Contract Law* (Oxford, 1995), 57; A. Burrows, *The Law of Restitution* (2nd edn, London, 2002), chapter 7; D. Capper, (1998) 114 LQR 479; D. Capper, 'The Unconscionable Bargain in the Common Law World' (2010) 126 LQR 403; M. Conaglen, 'Duress, Undue Influence, and Unconscionable Bargains – The Theoretical Mesh' (1999) 18 NZULR 509; N. Enonchong, *Duress, Undue Influence and Unconscionable Dealing* (London, 2006); R. Goff and G. H. Jones, *The Law of Restitution* (7th edn, London, 2007), chapter 12; G. Virgo, *Principles of the Law of Restitution* (2nd edn, Oxford, 2006), chapter 10; S. Waddams, (1976) 39 MLR 369; for references to other common law jurisdictions on this topic, see A. Phang, 'Doctrine and Fairness in the Law of Contract' (2009) 29 LS 534, 570 ff, and D. Capper, 'The Unconscionable Bargain in the Common Law World' (2010) 126 LQR 403.

153 [1983] 1 WLR 87, 94–5 (not disturbed on appeal, [1985] 1 WLR 173, CA); considered by Blair J in *Strydom v. Vendside Ltd* [2009] EWHC 2130 (QB); [2009] 6 Costs LR 886, at [34] to [39].

154 [1979] Ch 84, 110.

The modern English doctrine of ‘unconscionability’ or ‘exploitation’ is now unified. But, in the nineteenth century, there were two streams:¹⁵⁵ first, protection of ‘expectant’ heirs against exploitation;¹⁵⁶ secondly, protection of ‘poor, ignorant and necessitous’ persons.¹⁵⁷

11.37 ‘Unconscionability’ or ‘exploitation’ consists of four factors:

- (1) the vulnerable party’s special or serious disadvantage;
- (2) actual or constructive fraud (the element of conscious and reprehensible exploitation);
- (3) highly disadvantageous or ‘oppressive’¹⁵⁸ terms (the element of substantive economic harm); and
- (4) lack of independent advice¹⁵⁹ (as Capper notes, this fourfold analysis has also been articulated in Canada).¹⁶⁰

As for factors (1) to (3), in *Alec Lobb (Garages) Ltd v. Total Oil GB Ltd* (1983), Millett J explained:¹⁶¹

First, one party has been at a serious disadvantage to the other, whether through poverty, or ignorance, or lack of advice, or otherwise [almost certainly including alcoholic intoxication¹⁶² but only possibly – although the doubt seems misplaced – extending to narcotic addiction],¹⁶³ so that circumstances existed of which unfair advantage

155 A. Burrows, *The Law of Restitution* (2nd edn, London, 2002), 261 ff.

156 *Earl of Aylesford v. Morris* (1873) LR 8 Ch App 484 (citing Lord Hardwicke in *Earl of Chesterfield v. Janssen* (1751) 2 Ves Sen 125, 157); *O’Rorke v. Bolinbroke* (1877) LR 2 App Cas 814, 835, HL; cf *Tate v. Williamson* (1866) LR 2 Ch App 55 (undue influence between a distant relative and financial manager and a very young man who died at 24 from excessive drinking); and see the cases cited in *Fry v. Lane* (1888) 40 Ch D 312, 320.

157 *Fry v. Lane* (1888) 40 Ch D 312, Kay J: ‘poor man with imperfect education’ (citing *Evans v. Llewellyn* (1781) 1 Cox 333; 2 Bro CC 150, two journeymen exploited by their social superior; and *Haygarth v. Wearing* (1871) LR 12 Eq 320, Wickens V-C, schoolmistress swindled by brother); *Cresswell v. Potter* (note) [1978] 1 WLR 255, Megarry J; on the history, see J. L. Barton, (1987) 103 LQR 118.

158 The terms must be oppressive to the complainant, as distinct from being generally reprehensible, as emphasised in *Strydom v. Vendside Ltd* [2009] EWHC 2130 (QB); [2009] 6 Costs LR 886, at [39], *per* Blair J.

159 A. Burrows, *The Law of Restitution* (2nd edn, London, 2002), 260, noted by N. Bamforth, [1995] LMCLQ 538, 547 ff; Bamforth cites *Hart v. O’Connor* [1985] AC 1000, 1027–8, PC; *Multiservice Bookbinding v. Marden* [1979] Ch 84, 105, Browne-Wilkinson J; *Alec Lobb v. Total Oil* [1985] 1 WLR 173, CA; and *Boustany v. Pigott* (1993) 69 P & CR 298, PC (considered by Arden J in *J A Pye (Oxford) Estates v. Ambrose* [1994] NPC 53).

160 D. Capper, (2010) 126 LQR 403, 415, noting Cote J’s formulation in *Cain v. Clarica Life Insurance* (2005) 263 DLR (4th) 368, at [32] (Alberta Supreme Court) (criteria approved also in Ontario, D. Capper, (2010) 126 LQR 403 at n. 96).

161 [1983] 1 WLR 87, 94–5 (not disturbed on appeal, [1985] 1 WLR 173, CA); note also the Australian doctrine of ‘unconscionability’: *Commercial Bank of Australia Ltd v. Amadio* (1983) 151 CLR 447; *Louth v. Diprose* (1992) 175 CLR 621, High Court of Australia; *Garcia v. National Australia Bank Ltd* (1998) 194 CLR 395, High Court of Australia (on the last two cases, see A. Burrows, *The Law of Restitution* (2nd edn, London, 2002), 266–7); and see *Nichols v. Jessup* [1986] NZLR 226.

162 As for drunkenness, the point is cast iron in Australia, where judicial cognisance of extreme drunkenness has a long history: *Blomley v. Ryan* (1956) 99 CLR 362.

163 As for narcotic addiction, the point was left open (unnecessarily negatively) in *Irvani v. Irvani* [2000] 1 Lloyd’s Rep 412, 425, CA, *per* Buxton LJ, who said: ‘*Black v. Wilcox* (1976) 70 DLR (2d) 192 (Canada) ... espouses a broad doctrine of unconscionability, for instance in cases where, as in that case, one of the parties was addicted to drugs. I however agree with Chitty ... that this and other Commonwealth cases

could be taken ... Second, this weakness of the one party has been exploited by the other in some morally culpable manner ... And third, the resulting transaction has been not merely hard or improvident but overreaching and oppressive. Where there has been a sale at an undervalue, the undervalue has almost always been substantial, so that it calls for explanation,¹⁶⁴ and is in itself indicative of the presence of some fraud, undue influence, or some other feature.

Factor (1) was ‘updated’ by Megarry J in *Cresswell v. Potter* (decided in 1968, but reported in 1978).¹⁶⁵ He showed that ‘poverty’ does not require destitution, and ‘ignorance’ does not mean a low ‘IQ’:

[T]he euphemisms of the 20th century may require the word ‘poor’ to be replaced by ‘a member of the lower income group’ or the like, and the word ‘ignorant’ by ‘less highly educated’. The plaintiff has been a van driver for a tobacconist, and is a Post Office telephonist. [She] may properly be described as ‘poor’ ... I do not think that ‘poverty’ is confined to destitution. Further, although no doubt it requires considerable alertness and skill to be a good telephonist, I think that a telephonist can properly be described as ‘ignorant’ in the context of property transactions in general and the execution of conveyancing documents in particular.

And, in Canada, factor (1) has been held to embrace these various forms of transactional vulnerability: ‘an overwhelming imbalance in bargaining power caused by the victim’s ignorance of business, illiteracy, ignorance of the language of the bargain, blindness, deafness, illness, senility, or similar disability’.¹⁶⁶

As for factor (2), the element of exploitation, Lord Templeman in the Privy Council in *Boustany v. Pigott* (1995)¹⁶⁷ noted that there must be some unconscionable or extortionate abuse of power, some unfair taking advantage of a weaker party’s disabling condition or circumstances.¹⁶⁸ It is not enough that there was unequal bargaining power between the parties. More generally, Capper has listed English reported decisions since the 1970s in which unconscionability has been held not to apply to the relevant facts, or, where this doctrine *was* considered, it was overshadowed by the pleading of another doctrine.¹⁶⁹

do or may go beyond the limits of present English authority. Careful analysis would be required if the question of applying them in this jurisdiction were a live one.’

164 As noted at 11.27, this phrase is now used, in the context of undue influence, as the better way of expressing the notion of ‘manifest disadvantage’ (the latter label has now been discarded, except by Lord Millett in *National Commercial Bank (Jamaica) Ltd v. Hew* [2003] UKPC 51, at [33]).

165 (1968): (note) [1978] 1 WLR 255, 257–8.

166 D. Capper, (2010) 126 LQR 403, 415, noting Cote J’s formulation in *Cain v. Clarica Life Insurance* (2005) 263 DLR (4th) 368, at [32] (Alberta Supreme Court) (criteria approved also in Ontario, D. Capper, (2010) 126 LQR 403 at n. 96).

167 (1995) 69 P & CR 298, 303.

168 Citing, among other decisions, *Hart v. O’Connor* [1985] AC 1000, PC; *Commercial Bank of Australia v. Amadio* (1983) 46 ALR 402, 413, High Court of Australia; *Nichols v. Jessup* [1986] NZLR 226; *Louth v. Diprose* (1992) 175 CLR 621, High Court of Australia; *Garcia v. National Australia Bank Ltd* (1998) 194 CLR 395, High Court of Australia (on the last two cases, see A. Burrows, *The Law of Restitution* (2nd 2002), at 266–7).

169 D. Capper, (2010) 126 LQR 403, 406–7, noting these cases: *Burmah Oil Co. v. Bank of England*, *The Times*, 4 July 1981, Ch; *Watkin v. Watson-Smith*, *The Times*, 3 July 1986; *Irvani v. Irvani* [2000] 1

11.38 *Relationship between unconscionability and undue influence.* There are two points. First, the unconscionability doctrine does not apply to gifts, but only to transactions for value, or to deeds, according to a first instance case, *Langton v. Langton* (1995)¹⁷⁰ (although Capper has challenged this).¹⁷¹ By contrast, undue influence is available to invalidate gifts: for example, *Allcard v. Skinner* (1887) (gift of all worldly goods by a novice to a convent: see 11.24).¹⁷² Secondly, the task of delineating the borderline between undue influence and unconscionability, and the related question of possibly merging these doctrines, have generated much academic discussion.¹⁷³ Buxton LJ in *Irvani v. Irvani* (2000)¹⁷⁴ noted the fact that unconscionability does not require proof of a *vulnerable relationship*; whereas undue influence (11.23) generally (perhaps necessarily) does arise from a relationship of influence. It might be argued (such is the haziness of this category of equity) that *perhaps* actual influence might be ‘committed out of the blue’ between parties who are hitherto unconnected and who enter into a transaction without any prior ‘recognised’ or ‘presumed’ relationship between the parties, one party subtly taking undue advantage of the other. But, first, this approach seems redundant, because such a complaint should be better accommodated (depending on the particular facts) as fraudulent misrepresentation, or unconscionability, or duress. And, as a matter of pure principle, it is submitted that the courts should state that undue influence requires *exploitation of a relationship subsisting independently of the gift or transaction (or independently of the stage of the transaction) which is now impugned*. The underlined parenthesis accommodates the unusual situation, examined in *Macklin v.*

Lloyd’s Rep 412, CA; *Portman Building Society v. Dusangh* [2000] 2 All ER (Comm) 221, CA (noted by L. McMurtry, [2000] Conv 573); *Jones v. Morgan* [2001] Lloyd’s Rep Bank 323 (noted by J. Devenney, [2002] JBL 539); *Kalsep Ltd v. X-Flow BV*, *The Times*, 3 May 2001, Ch; *Humphreys v. Humphreys* [2004] EWHC 2201 (Ch); [2005] 1 FCR 712 (and see now, *Strydom v. Vendside Ltd* [2009] EWHC 2130 (QB); [2009] 6 Costs LR 886).

170 [1995] 3 FCR 521, 538–40; *The Times*, 24 February 1995, A. W. H. Charles QC, sitting in the Chancery Division (quoted without disapproval in a *dictum* in *Randall v. Randall* [2004] EWHC 2258 (Ch); [2005] 1 P & CR DG 4).

171 D. Capper, (2010) 126 LQR 403, 406.

172 *Allcard v. Skinner* (1887) 36 Ch D 145, 183, CA.

173 P. Birks and N. Y. Chin, ‘On the Nature of Undue Influence’, in J. Beatson and D. Friedmann (eds.), *Good Faith and Fault in Contract Law* (Oxford, 1995), 57, especially at 57–60, 63–5, 85–8, 92–7; Bigwood’s discussion of Birks and Chin: R. Bigwood, ‘Contract and the Liberal Conception of Contract: Observing Basic Distinctions Part II’ (2000) 16 *Journal of Contract Law* 191, 200; R. Bigwood, *Exploitative Contracts* (Oxford, 2003), 467 ff; R. Bigwood, ‘Contracts by Unfair Advantage: From Exploitation to Transactional Neglect’ (1995) 16 OJLS 503; P. Birks, [1997] *Restitution Law Review* 72, 76 n. 20; P. Birks, ‘Undue Influence as Wrongful Exploitation’ (2004) 120 LQR 34–7; D. Capper, ‘Undue Influence and Unconscionability: A Rationalisation’ (1998) 114 LQR 479; D. Capper, ‘The Unconscionable Bargain in the Common Law World’ (2010) 126 LQR 403, 416–19; M. Chen-Wishart, ‘Undue Influence: Beyond Impaired Consent and Wrongdoing towards a Relational Analysis’, in A. Burrows and A. Rodger (eds.), *Mapping the Law: Essays in Memory of Peter Birks* (Oxford, 2006); M. Chen-Wishart, ‘Undue Influence: Vindicating Relationships of Influence’ [2006] CLP 231; M. Conaglen, ‘Duress, Undue Influence, and Unconscionable Bargains – The Theoretical Mesh’ (1999) 18 NZULR 509; J. P. Devenney and A. Chandler, ‘Unconscionability and the Taxonomy of Undue Influence’ [2007] JBL 541, at 560–1; N. Enonchong, *Duress, Undue Influence and Unconscionable Dealing* (London, 2006), 349–50; A. Mason, ‘The Place of Equity and Equitable Doctrines in the Contemporary Common Law World – An Australian Perspective’, in D. Waters (ed.), *Equity, Fiduciaries and Trusts* (Toronto, 1993); L. McMurtry, ‘Unconscionability and Undue Influence: An Interaction?’ [2000] Conv 573; A. Phang and H. Tjio, ‘The Uncertain Boundaries of Undue Influence’ [2002] LMCLQ 231.

174 [2000] 1 Lloyd’s Rep 412, CA.

Dowsett (2004)¹⁷⁵ (11.28), where, during the course of a transaction, one party acquires ascendancy over the other, even though before this the parties were strangers, and the culmination of a series of dealings is that a weaker party enters into an arrangement that ‘calls for explanation’. It is then open to rescission on the ground of presumed undue influence unless the stronger party can show that the weaker party exercised a free and informed mind at that point.

Buxton LJ’s discussion in *Irvani v. Irvani* (2000) of this doctrinal distinction certainly emphasises the ‘relational quality’ of undue influence across both the ‘actual undue influence’ and ‘presumed undue influence’ categories. His discussion justifies extensive citation:¹⁷⁶

Undue influence is concerned with the prior relationship between the contracting parties, and with whether that was the motivation or reason for which the bargain was entered into. Unconscionable bargain is, as its title suggests, concerned with the nature and circumstances of the bargain itself, and can arise without there being any relationship, outside that of the immediate contract, between the parties.

He added:

It is particularly important to keep these distinctions clear, because otherwise there may be a tendency to think that a case that has some elements of undue influence, but is not in law a case of undue influence; and which has some elements of unconscionable bargain, but which is not in law a case of unconscionable bargain; can by the combination of these different and inadequate claims be turned into a case that attracts relief on a vaguer basis of general equity.

As for the context in the immediate case (a party’s drug addiction), he said:

It is also important to keep the distinctions clear when one of the circumstances claimed to attract relief is that one of the parties to the contract was suffering from mental incapacity, or addiction to drink or drugs. It is doubtful whether that circumstance can, of itself, give rise to a claim of undue influence.

- 11.39 So-called ‘gross disparity’, a principle rather similar to the English equitable doctrine of unconscionability, has been adopted in Article 3.10 of UNIDROIT’s *Principles of International Commercial Contracts* (2004):¹⁷⁷

A party may avoid the contract or an individual term of it if, at the time of the conclusion of the contract, the contract or term unjustifiably gave the other party an excessive advantage. Regard is to be had, among other factors, to (a) the fact that

175 [2004] EWCA Civ 904; [2004] 2 EGLR 75; [2004] 34 EG 68; [2005] WTLR 1561.

176 [2000] 1 Lloyd’s Rep 412, 424, CA.

177 2nd edn, Rome, 2004; see M. J. Bonell (ed.), *The UNIDROIT Principles in Practice: Case Law and Bibliography on the UNIDROIT Principles of International Commercial Contracts* (2nd edn, Ardsley, NY, 2006), 207 ff; S. Vogenauer and J. Kleinheisterkamp (eds.), *Commentary on the UNIDROIT Principles of International Commercial Contracts* (Oxford, 2009), 449 ff.

the other party has taken unfair advantage of the first party's dependence, economic distress or urgent needs, or of its improvidence, ignorance, inexperience or lack of bargaining skill, and (b) the nature and purpose of the contract.

But, as the comment to this principle adds: 'Superior bargaining power due to market conditions alone is not sufficient.'

5. SUBSTANTIVELY UNFAIR BARGAINS¹⁷⁸

11.40 In *Hart v. O'Connor* (1985), Lord Brightman distinguished 'procedural' and 'substantive' unfairness:¹⁷⁹

If a contract is stigmatised as 'unfair', it may be unfair in one of two ways. It may be unfair by reason of the unfair manner in which it was brought into existence; a contract induced by undue influence is unfair in this sense. It will be convenient to call this 'procedural unfairness'. It may also, in some contexts, be described (accurately or inaccurately) as 'unfair' by reason of the fact that the terms of the contract are more favourable to one party than to the other. In order to distinguish this 'unfairness' from procedural unfairness, it will be convenient to call it 'contractual imbalance'. The two concepts may overlap. Contractual imbalance may be so extreme as to raise a presumption of procedural unfairness, such as undue influence or some other form of victimisation. Equity will relieve a party from a contract which he has been induced to make as a result of victimisation. Equity will not relieve a party from a contract on the ground only that there is contractual imbalance not amounting to unconscionable dealing.

Duress and undue influence, for example, involve 'procedural unfairness'. Both are grounds of invalidity reflecting the fact that a party's consent to the agreement has been unsatisfactorily given. Such an attack on the integrity of a party's consent is to be contrasted with legal challenges based on the extreme one-sidedness of the bargain, or based on the fact that a particular obligation is draconian. Lord Brightman, in the passage quoted above, acknowledged that the mere fact that a contract is economically disadvantageous towards one party does not justify setting aside or readjusting that transaction. Indeed, it is a basic rule (5.19) that the English courts 'do not weigh the adequacy of consideration' (in English contract law there is no general doctrine of *laesio enormis* (*lésion*, in French) nor a concept of fair exchange; nor in the relevant civilian systems does *lésion* apply to all species of contract, nor even to all sales).¹⁸⁰

178 S. Smith, (1996) 112 LQR 138; M. Trebilcock, 'The Doctrine of Inequality of Bargaining Power: Post-Benthamite Economics in the House of Lords' (1976) 26 *University of Toronto Law Journal* 359; and see also materials on the penalty jurisdiction, 19.02, and the deposit doctrine, 19.25; on the history, see J. L. Barton, (1987) 103 LQR 118.

179 [1985] AC 1000, 1024, PC.

180 Cf French law of this doctrine: Code Civil, Articles 1674 ff; B. Nicholas, *French Law of Contract* (2nd edn, Oxford, 1992), 137 ff; such a doctrine also applies in Jersey, *Snell v. Beadle* [2001] UKPC 5; [2001] 2 AC 304.

- 11.41 There are, however, exceptional situations where, according to English law, an agreement can be upset or revised because the transaction or relevant term is perceived as intrinsically too harsh, unfair or mischievous, for example: (1) the equitable penalty rule (19.02); (2) control of excessive deposits (see 19.32 (statute) and 19.38 (common law)); (3) the rule against unreasonable restraints of trade (20.20);¹⁸¹ (4) the Admiralty jurisdiction to relieve against extortionate maritime salvage agreements;¹⁸² (5) statutory protection against over-severe clauses exempting a party from liability (the Unfair Contract Terms Act 1977 (15.08)); (6) the statutory power to control overreaching consumer credit contracts;¹⁸³ and (7) the Unfair Terms in Consumer Contracts Regulations 1999 (15.08).

6. NO DOCTRINE OF 'INEQUALITY OF BARGAINING POWER'

- 11.42 In *Lloyds Bank Ltd v. Bundy* (1975), Lord Denning MR attempted to fashion a theory of 'inequality of bargaining power' suggesting that this doctrine could be extracted from the medley of particular doctrines examined in the earlier sections of this chapter¹⁸⁴ (for the majority's approach, see 11.30). His new theory involved an interweaving of three strands: (1) procedural and (2) substantive unfairness, and (3) the concept of 'inequality of bargaining power'. Having reviewed various doctrines – duress, undue influence, unconscionability, and relief against extortionate maritime salvage agreements¹⁸⁵ – he ventured the following bold synthesis:

Gathering all together, I would suggest that through all these instances there runs a single thread. They rest on 'inequality of bargaining power'. By virtue of it, the English law gives relief to one who, without independent advice, enters into a contract upon terms which are very unfair or transfers property for a consideration which is grossly inadequate, when his bargaining power is grievously impaired by reason of his own needs or desires, or by his own ignorance or infirmity, coupled with undue influences or pressures brought to bear on him by or for the benefit of the other.

- 11.43 But Lord Denning's 'inequality of bargaining power' doctrine, just summarised, was the minority approach in the *Bundy* case (for the majority's approach, see 11.30). And his bold proposal was rejected in later case law as too vague, and hence commercially unattractive.¹⁸⁶ This rejection is sound, for the following reasons. First, the proposal was a mix of concepts: (1) coercion, improper influence, and exploitation, (2) substantive

181 E.g. *Schroeder v. MacCaulay* [1974] 1 WLR 1308, HL (young songwriter's improvident bargain).

182 *Akerblom v. Price* (1881) 7 QBD 129, 133, CA; '*The Port Caledonia*' and '*The Anna*' [1903] P 184 (topic now regulated by section 224 of and Schedule 11 to the Merchant Shipping Act 1995; this allows a proper reward to be granted if the agreement is unfair); on the admiralty jurisdiction, see also the comments of Lord Denning MR in *Lloyds Bank Ltd v. Bundy* [1975] QB 326, 339, CA; the jurisdiction does not extend to non-tidal waters: '*The Goring*' [1988] AC 831, HL.

183 Sections 140A and 140B of the Consumer Credit Act 1974 (inserted by section 19 of the Consumer Credit Act 2006), imposing a criterion of unfairness in favour of the debtor.

184 [1975] QB 326, 337–40, CA.

185 See note 182 above.

186 Notably, by Lord Scarman in *National Westminster Bank v. Morgan* [1985] AC 686, 708, HL; see also the discussion in the current paragraph of the text.

unfairness, and (3) inequality of bargaining power. This looks like a mongrel doctrine. Secondly, the proposal would introduce a manifestly high level of uncertainty:¹⁸⁷ 'Inequality of bargaining power must anyhow be a relative concept. It is seldom in any negotiation that the bargaining powers of the parties are absolutely equal.'¹⁸⁸ Thirdly, legislation is the preferred method of countering this type of problem: whether an 'unfair' imbalance subsists in consumer contracts is now extensively determined by the Unfair Terms in Consumer Contracts Regulations 1999 (15.33). The Unfair Contract Terms Act 1977 is another important source of protection, in the context of exclusion clauses (15.08). As noted by Lord Scarman in *National Westminster Bank plc v. Morgan* (1985)¹⁸⁹ and Steyn LJ in *CTN Cash & Carry Ltd v. Gallahers* (1994),¹⁹⁰ Parliament has in modern times sought to control some of the worst instances of economic oppression or imbalance. The courts regard the possibility of regulating contracts by reference to market imbalance and substantive harshness as a delicate task, even a quasi-political one. For this reason, and in the interest of precision, such regulation¹⁹¹ is better undertaken by legislation. Good examples are the power to re-open extortionate credit transactions under the Consumer Credit Act 1974¹⁹² and the complex UK and European Union schemes for countering anti-competitive practices and for controlling monopolies.¹⁹³

187 Cf in another context (relief against forfeiture of proprietary interests) Lord Hoffmann's convincing warning against introducing uncertainty into commercial law through an over-extension of equitable discretion: *Union Eagle Ltd v. Golden Achievement Ltd* [1997] AC 514, 519D, 523, PC: 17.40.

188 *Alec Lobb Garages Ltd v. Total Oil Great Britain Ltd* [1985] 1 WLR 173, 183, CA, per Dillon LJ.

189 [1985] AC 686, 708, HL.

190 [1994] 4 All ER 714, 718–19, CA.

191 H. G. Collins, *Regulating Contracts* (Oxford, 1999).

192 Sections 137–140 of the Consumer Credit Act 1974; applied in *Paragon Finance plc v. Nash* [2002] 1 WLR 685, CA, at [49] to [68] (note the lacuna identified at [67]); see now new sections 140A and 140B of the Consumer Credit Act 1974, inserted by section 19 of the Consumer Credit Act 2006, imposing a broad criterion of unfairness in favour of the debtor.

193 *Chitty on Contracts* (30th edn, London, 2008), chapter 21; and *Bellamy and Child's European Community Law of Competition* (6th edn, London, 2007).

VI

Terms and interpretation

Chapter contents

1. Classification of terms: a guide to discussion in other parts of this work *para.* 12.01
2. Ancillary agreements or clauses *para.* 12.03

12

Terms in general

1. CLASSIFICATION OF TERMS: A GUIDE TO DISCUSSION IN OTHER PARTS OF THIS WORK

12.01 Summary of main points

The main types of contractual terms are summarised in the next paragraph, and that summary will enable cross-references to be made to discussion elsewhere in this book. The remainder of this chapter (12.03 ff below) will then be devoted to various 'ancillary clauses' commonly used in commercial documents.

Terms in general

A. Burrows and E. Peel (eds.), *Contract Terms* (Oxford, 2007)

K. Wedderburn, 'Collateral Contracts' [1959] CLJ 58

See also chapter 13 on implied terms; and chapter 15 on exclusion clauses.

Specific clauses

N. Andrews, *Contracts and English Dispute Resolution* (Tokyo, 2010), chapters 21 and 22, for a succinct introduction to arbitration and mediation (including clauses providing for these forms of dispute resolution)

K. P. Berger, 'Law and Practice of Escalation Clauses' (2006) 22 *Arbitration International* 1–17

A. Briggs, *Agreements on Jurisdiction and Choice of Law* (Oxford, 2008)

L. Gulliver, 'Retention of Title Clauses: A Question of Balance', in A. Burrows and E. Peel (eds.), *Contract Terms* (Oxford, 2007), chapter 14

D. Joseph, *Jurisdiction and Arbitration Agreements and Their Enforcement* (London, 2005)

S. Nesbitt and H. Quinlan, 'The Status and Operation of Unilateral or Optional Arbitration Clauses' (2006) 22 *Arbitration International* 133

S. Rowan, 'For the Recognition of Remedial Terms Agreed Inter Partes' (2010) 126 LQR 448
 S. Whittaker, 'Termination Clauses', in A. Burrows and E. Peel (eds.), *Contract Terms* (Oxford, 2007), chapter 13

12.02 Terms are promissory or non-promissory, express or implied (for comments on the variety of 'promises', see 1.12). On these and related points, the reader is referred to other parts of this work, as indicated:

- (1) classification of promissory obligations: conditions; innominate (or 'intermediate') terms, and warranties: 17.18 ff
- (2) non-promissory terms: these are terms which prevent the contract from operating (so-called 'conditions precedent'): 1.16, 10.07, 10.10, 14.29; or which cause the contract to terminate ('conditions subsequent'): 10.11; as well as termination clauses:¹ 16.30, 17.04
- (3) the distinction between a misrepresentation and a promissory term: 9.22
- (4) the possibility that a statement might be treated as both a misrepresentation and a contractual term: 9.25
- (5) criteria for determining whether a pre-contractual assurance has effect as a contractual term: 9.07
- (6) collateral warranties: 9.05 to 9.10
- (7) implied terms: 13.01 ff
- (8) incorporation of terms: 15.02
- (9) the parol evidence rule: 14.26
- (10) entire agreement clauses: 9.27
- (11) non-reliance clauses: 9.28 ff
- (12) exclusion clauses in general: 15.01 ff; and for *exclusion clauses and misrepresentation*: 9.26 ff
- (13) unfair terms in general: 15.08 ff
- (14) interpretation of written contracts: 14.01 ff
- (15) agreements to negotiate: English law does not recognise an agreement to bargain or negotiate in good faith (see 2.07 on *Walford v. Miles* (1992));² but the following (2.08 ff) are valid, provided the promise is supported by consideration: (i) a 'lock-out' or 'exclusivity' agreement *for a specified period*³ not to deal or negotiate with outsiders, but only to negotiate with the other party; (ii) an agreement to procure a third party's permission (for example, planning permission or an export licence), by taking 'reasonable' or 'best endeavours'⁴

1 S. Whittaker, 'Termination Clauses', in A. Burrows and E. Peel (eds.), *Contract Terms* (Oxford, 2007), chapter 13.

2 [1992] 2 AC 128, HL; P. Neill, (1992) 108 LQR 405; A. Berg, (2003) 110 LQR 357; also invalid is an agreement to use best or reasonable endeavours to reach agreement on the subject matter or the price: *Little v. Courage* (1995) 70 P & CR 469, 476, CA, *per* Millett LJ.

3 *Walford v. Miles* [1992] 2 AC 128, HL, applied in *Pitt v. PHH Asset Management Ltd* [1994] 1 WLR 327, CA.

4 *Walford v. Miles* [1992] 2 AC 128, HL, and *Little v. Courage* (1995) 70 P & CR 469, 476, CA, both acknowledge this.

- (16) *force majeure* clauses: such a clause declares when a party will be released from his obligations, or excused from liability for default, by reason of freak and excusable supervening events⁵ (16.09, considering *Thames Valley Power Ltd v. Total Gas & Power Ltd* (2005));⁶ and 16.19, for reference to the clause in '*The Super Servant Two*' (1990))
- (17) retention of title clauses: these operate to confer security on vendors⁷
- (18) express repayment clauses: 17.04
- (19) liquidated damages clauses: 19.02
- (20) clauses stipulating party preference for the 'cost of cure' measure of damages: it appears that these might be valid, at least in some contexts: 18.27
- (21) deposits: 19.27
- (22) profit-disgorgement clauses: it appears that these might be valid, at least in some contexts: 18.56
- (23) stipulations indicating party preference for specific performance or injunctive relief: English law has yet to accept these as valid because they might usurp judicial discretionary control of this coercive form of relief: 18.18, 18.20.

2. ANCILLARY AGREEMENTS OR CLAUSES

12.03 Collateral warranties and *force majeure*, entire agreement, non-reliance, and exclusion clauses are discussed elsewhere (9.05 to 9.10). In the ensuing paragraphs, other types of ancillary clauses will be briefly examined.

12.04 *Agreements 'subject to contract', 'letters of comfort' and 'letters of intent'*. See also 1.16, 2.07, 4.21, 5.05, 6.06. Such a provision expressly negatives an intention to create legal relations. And so a party acts at his own financial risk if he performs during the phase when an agreement is 'subject to contract'.⁸ The position changes, however, if the other party expressly undertakes, or otherwise makes clear, that performance will be remunerated. For example, in *William Lacey (Hounslow) Ltd v. Davis* (1957), Barry J awarded a *quantum meruit* (a restitutionary claim for the value of services rendered: see 18.55) in favour of a party who had been clearly encouraged, for unspecified reward, by the other to prepare detailed plans for the rebuilding of a site.⁹ Furthermore, the Supreme Court in

5 E. McKendrick (ed.), *Force Majeure and Frustration of Contract* (2nd edn, London, 1995), especially at 34; E. McKendrick, 'The Regulation of Long-Term Contracts in English Law', in J. Beatson and D. Friedmann (eds.), *Good Faith and Fault in Contract Law* (Oxford, 1995), 305, 323 ff; E. McKendrick, 'Force Majeure Clauses: The Gap between Doctrine and Practice', in A. Burrows and E. Peel (eds.), *Contract Terms* (Oxford, 2007), chapter 12; *Chitty on Contracts* (30th edn, London, 2008), 14–137 ff.

6 [2005] EWHC 2208 (Comm); [2006] 1 Lloyd's Rep 441.

7 L. Gulliver, 'Retention of Title Clauses: A Question of Balance', in A. Burrows and E. Peel (eds.), *Contract Terms* (Oxford, 2007), chapter 14; for a convenient summary, see *Atiyah's Sale of Goods* (12th edn, London, 2010), 12–13.

8 E.g. *Regalian Properties Ltd v. London Docklands Development Corporation* [1995] 1 WLR 212, Rattee J; similarly, no estoppel found where negotiations were 'subject to contract', *Attorney-General of Hong Kong v. Humphrey's Estate Ltd* [1987] AC 114, PC; but cf the special facts of *Salvation Army Trustee Co. Ltd v. West Yorkshire Metropolitan County Council* (1980) 41 P & CR 179.

9 [1957] 1 WLR 932, Barry J.

RTS Flexible Systems Ltd v. Molkerei Alois Müller GmbH (2010)¹⁰ held that a ‘subject to contract’ provision can cease to govern the parties’ dealings if there has been a consensual waiver of that bar upon contractual enforceability, and that such a waiver can be manifested by conduct (4.21). For the Court of Appeal’s recognition of an implied ‘subject to contract’ arrangement, see the discussion at 6.06 of *Grant v. Bragg* (2009).¹¹ ‘Letters of comfort’ are examined at 6.13, notably the clear statement by Sir Anthony Clarke MR in *Associated British Ports v. Ferryways NV* (2009) that they are not binding¹² (6.13 also contains references to ‘letters of intent’; and see also 2.04).

- 12.05 *Choice-of-law clauses*.¹³ See also 9.24 and 17.48. Such a clause specifies which national system of contract law will apply to the transaction: for details, see *Dicey, Morris and Collins*¹⁴ and Briggs.¹⁵ The parties can thus exclude an undesirable national system of contract law, or specify a neutral contractual system (neutral, that is, by reference to the parties’ nationality, domicile or place of business).
- 12.06 *Mediation agreements*.¹⁶ Parties will often agree that they will mediate in good faith before formal litigation or arbitration. Colman J in *Cable & Wireless plc v. IBM UK* (2002)¹⁷ (2.13) upheld such a mediation clause. He held that, in the face of such an undertaking, a party’s decision to bypass mediation is a breach of the dispute-resolution agreement. He granted a stay upon premature court litigation, thus requiring the parties to reconsider mediation.
- 12.07 *Jurisdiction clauses*.¹⁸ See also 17.65 and 17.66. An exclusive jurisdiction clause stipulates that legal disputes arising from the relevant transaction can only be litigated in the nominated jurisdiction, for example the courts of London or Hong Kong. A non-exclusive jurisdiction clause confers jurisdiction on the relevant nominated courts even though, in the absence of such a clause, that jurisdiction would not have been available to the parties.¹⁹

10 [2010] UKSC 14; [2010] 1 WLR 753.

11 [2009] EWCA Civ 1228; [2010] 1 All ER (Comm) 1166, at [28] to [32], *per* Lord Neuberger MR.

12 [2009] EWCA Civ 189; [2009] 1 Lloyd’s Rep 595, at [24] to [27], *per* Sir Anthony Clarke MR.

13 A. Briggs, *Agreements on Jurisdiction and Choice of Law* (Oxford, 2008); A. Briggs, in A. Burrows and E. Peel (eds.), *Contract Terms* (Oxford, 2007), chapter 15; on the Rome I Regulation, see *Chitty on Contracts* (first supplement to the 30th edn, 2010), 30–131, citing academic commentary on Regulation (EC) No. 593/2008 (effective in the UK on 17 December 2009).

14 *Dicey, Morris and Collins, The Conflict of Laws* (14th edn, London, 2006), 32–01 ff.

15 A. Briggs, *ibid.*, at chapters 10 and 11.

16 K. P. Berger, ‘Law and Practice of Escalation Clauses’ (2006) 22 *Arbitration International* 1–17; for a succinct introduction to mediation, see N. Andrews, *Contracts and English Dispute Resolution* (Tokyo, 2010), chapter 22.

17 *Cable & Wireless plc v. IBM United Kingdom Ltd* [2002] 2 All ER (Comm) 1041, Colman J.

18 A. Briggs, *Agreements on Jurisdiction and Choice of Law* (Oxford, 2008); D. Joseph, *Jurisdiction and Arbitration Agreements and Their Enforcement* (London, 2005); for a succinct introduction to arbitration, see N. Andrews, *Contracts and English Dispute Resolution* (Tokyo, 2010), chapter 21.

19 *Deutsche Bank AG v. Highland Crusader Offshore Partners LP* [2009] EWCA Civ 725; [2010] 1 WLR 1023, at [50], [64], [105] and [106].

12.08 Arbitration clauses. See also 12.11.²⁰ The Arbitration Act 1996 requires an arbitration agreement to be in writing.²¹ Arbitration agreements concern agreements ‘to submit to arbitration present or future disputes’, and these include ‘differences’.²² In *Premium Nafta Products Ltd v. Fili Shipping Co. Ltd* (2007), the House of Lords held that, in accordance with the principle of ‘separability’ (acknowledged by section 7 of the Arbitration Act 1996), the invalidity of the main contract does not necessarily entail the invalidity of the arbitration agreement.²³ The arbitration clause will be invalid only if both the main contract and the arbitration clause are the product of forgery, or ‘if a party alleges that someone who purported to sign [the main contract and arbitration clause] as agent on his behalf had no authority whatever to conclude any agreement on his behalf’.²⁴

12.09 Inability to issue anti-suit injunction within European jurisdiction zone to ensure compliance with a jurisdiction or arbitration clause: *Turner v. Grovit* and *The West Tankers* case. Outside ‘Europe’ (that is, those EU Member States subscribing to the Jurisdiction Regulation,²⁵ or any non-EU jurisdictions party to the Lugano Convention on Jurisdiction and the Recognition and Enforcement of Judgments in Civil and Commercial Matters),²⁶ the English courts’ hands are untied (see (1) below); but, within ‘Europe’, as we shall now see, the European Court of Justice has twice applied the shackles (see (2) and (3) below).

- (1) *Jurisdiction clauses generally.* To look first beyond ‘Europe’, an English anti-suit injunction can still be granted to prevent a person from bringing, or continuing to pursue, *non-European* (see the text below) proceedings (in court or otherwise) brought in breach of an exclusive jurisdiction clause²⁷ or arbitration clause (for example, a

20 D. Joseph, *Jurisdiction and Arbitration Agreements and Their Enforcement* (London, 2005); an agreement to arbitrate is subject to the traditional analysis of repudiatory breach and ‘acceptance’ by the innocent party: J. Levy, (2007) NLJ 1036, noting *Bea Hotels NV v. Bellway LLC* [2007] EWHC 1363 (Comm), Cooke J, and *Downing v. Al Tameer Establishment* [2002] EWCA Civ 721, at [21], [25] and [26], also noting the seminal ‘contractual’ analysis of arbitration agreements in *Bremer Vulcan v. South India Shipping Corporation Ltd* [1981] AC 909, HL, ‘*The Hannah Blumenthal*’ [1983] 1 AC 854, HL, ‘*The Splendid Sun*’ [1981] QB 694, CA, and ‘*The Leonidas D*’ [1985] 1 WLR 925, CA (on this stream of authority, see M. Mustill and S. Boyd, *Commercial Arbitration: Companion Volume* (London, 2001), 503 ff).

21 Section 3 of the Arbitration Act 1996; M. Mustill and S. Boyd, *Commercial Arbitration: Companion Volume* (London, 2001), 16, and at 258 ff; for an important discussion of arbitration clauses affecting sovereign states, *Svenska Petroleum Exploration AB v. Government of the Republic of Lithuania* (No. 2) [2006] EWCA Civ 1529; [2007] 2 WLR 876, considering section 9(1) of the State Immunity Act 1978.

22 Sections 6(1) and 82(1) of the Arbitration Act 1996; M. Mustill and S. Boyd, *Commercial Arbitration: Companion Volume* (London, 2001), 22–3, suggesting that there is no discernible difference between these terms; noting, to the same effect, *Hayter v. Nelson and Home Insurance* [1990] 2 Lloyd’s Rep 265.

23 *Premium Nafta Products Ltd v. Fili Shipping Co. Ltd* [2007] UKHL 40; [2007] 4 All ER 951.

24 *Ibid.*, at [17] to [19].

25 Council Regulation (EC) No. 44/2001 of 22 December 2001 on ‘jurisdiction and the recognition and enforcement of judgments in civil and commercial matters’.

26 R. G. Fentiman, *International Commercial Litigation* (Oxford, 2010), 1.92, recording (in 2010) that only Norway has ratified the revised Lugano Convention: [2007] OJ L339/1, which took effect on 1 January 2010 (the other three European Free Trade Association jurisdictions, Switzerland, Liechtenstein, and Iceland, have yet to ratify); the 2007 Lugano Convention replaces the Lugano Convention of 16 September 1988.

27 *Deutsche Bank AG v. Highland Crusader Offshore Partners LP* [2009] EWCA Civ 725; [2010] 1 WLR 1023, at [50] ff, contains an eight-point distillation of principles concerning jurisdiction clauses and anti-suit relief.

- clause nominating English High Court litigation, or arbitration in London, in breach of which a party to the clause commences proceedings, court litigation or arbitration in, say, Buenos Aires). If the nominated forum is outside England (say, Tokyo or Sydney), but a party to the relevant clause commences English court proceedings in breach of this, the 'English litigation' defendant can seek a stay of those improper proceedings. Both the injunction and stay are subject to exceptions, notably if the relevant proceedings include parties or issues lying beyond the scope of the clause.²⁸ But, even here, some flexibility is possible. For example, in *Morgan Stanley & Co. International plc v. China Haisheng Juice Holdings Co. Ltd* (2009), an exclusive jurisdiction clause between M and C nominated England. H, M's affiliate, was also involved in the ensuing substantive dispute.²⁹ C sued both M (in breach of the jurisdiction clause) and H in China; and M sued C in England (in accordance with the jurisdiction clause). In the English Commercial Court, Teare J held that, although a dispute between C and H lay outside the M/C jurisdiction clause (to which H was not a party), to avoid conflicting Chinese and English decisions on the merits of these closely related pieces of litigation, it was necessary to issue an anti-suit injunction against C to restrain its Chinese proceedings against M. That injunction would be likely to induce C to abandon its proceedings against H in China and instead to relocate that part of its dispute as part of a counter-claim to the M/C proceedings in London.
- (2) *Jurisdiction clauses within the EU or for Lugano Convention countries.* The European Court of Justice's decision in *Turner v. Grovit* (2005)³⁰ prevents the English courts from issuing anti-suit injunctions to enforce exclusive English jurisdiction clauses where the offending court proceedings have been commenced within the European jurisdictional zone (Member States, in accordance with the Jurisdiction Regulation 2001, or, in the case of the Lugano scheme, Switzerland and Norway).³¹
 - (3) *Arbitration clauses.* A party to an arbitration agreement can slow down the intended process by bringing a pre-emptive case in the courts. In practice, it takes a long time for the courts to renounce jurisdiction in favour of an arbitrator. The European Court of Justice's decision in *Allianz SpA v. West Tankers* (2009)³² prevents the common law anti-suit injunction from being issued to counter breach of arbitration clauses by the commencement of inconsistent *court* litigation within the *same* European jurisdictional zone. For example, a clause might stipulate that disputes should be subject to arbitration in London. If a party to the clause improperly commences proceedings, whether court litigation or arbitration, in, say, Buenos Aires or New York or Moscow, the English Commercial Court, upholding a London arbitration clause,

28 *Donohue v. Armco Inc.* [2001] UKHL 64; [2002] 1 All ER 749, HL.

29 [2009] EWHC 2409 (Comm); [2010] 1 Lloyd's Rep 265.

30 *Turner v. Grovit* (Case C-159/02) [2005] 1 AC 101, ECJ; for comment, see N. Andrews, 'Abuse of Process and Obstructive Tactics under the Brussels Jurisdictional System ...' (2005) *European Community Private Law Review* 8–15 (this journal is also entitled *Zeitschrift für Gemeinschaftsprivatrecht* and *Revue de droit privé international*).

31 Council Regulation (EC) No. 44/2001 of 22 December 2001 on 'jurisdiction and the recognition and enforcement of judgments in civil and commercial matters'.

32 Case C-185/07 [2009] 1 AC 1138; [2009] 1 Lloyd's Rep 413 (noted by E. Peel, (2009) 125 LQR 365).

has held that there is:³³ ‘nothing in the European Court decision in the [*West Tankers* case] which impacts upon the law as developed in this country in relation to anti-suit injunctions which prevents parties from pursuing proceedings in the courts of a country which is *not* a Member State of the European Community [or of the Lugano system]’. Nor, as Teare J held in *Sheffield United Football Club Ltd v. West Ham United Football Club plc* (2008), is there any prohibition upon the grant of an anti-suit injunction to stop improper resort to *arbitration* proceedings.³⁴ However, the Court of Appeal held in *National Navigation Co. v. Endesa Generacion SA* (2009)³⁵ (after considering the ECJ’s decision in the *West Tankers* case) that, once a Member State court has declared whether an arbitration clause does or does not apply, and provided this decision counts as a ‘Regulation judgment’ (because it is ancillary to a substantive claim falling within the Jurisdiction Regulation 2001),³⁶ all Member State courts are obliged to recognise that decision. In the same decision, the Court of Appeal said that arbitrators would also be bound by such a decision, although on the distinct basis of the common law doctrine of issue estoppel.³⁷

- 12.10 *Hybrid arbitration and jurisdiction clauses.* These enable one party to opt out of court proceedings in England by taking the case to arbitration or, conversely, enable a party to opt out of arbitration and instead bring proceedings before an English court. The English High Court has upheld so-called ‘hybrid’ dispute-resolution clauses.³⁸
- 12.11 *Arbitration: finality clauses.* Care and precision are required to exclude under English law the qualified right of appeal on a point of law from an arbitration award to the English Commercial Court. In *Shell Egypt West Manzala GmbH v. Dana Gas Egypt Ltd* (2009),³⁹ Gloster J held that a clause stating that an arbitration award is ‘final, conclusive and binding’ is not an effective exclusion of a High Court appeal. By contrast, in *Sheffield United Football Club Ltd v. West Ham United Football Club plc* (2008),⁴⁰ Teare J held that an arbitration clause had explicitly excluded further review or appeal by a court of law; and he further held that the same clause did not by implication create a right to seek review by recourse to a higher level of arbitration.

33 *Shashoua v. Sharma* [2009] EWHC 957; [2009] 2 All ER (Comm) 477; [2009] 2 Lloyd’s Rep 376; [2009] 1 CLC 716, at [39], Cooke J.

34 [2008] EWHC 2855 (Comm); [2009] 1 Lloyd’s Rep 167.

35 [2009] EWCA Civ 1397; [2010] 1 Lloyd’s Rep 193; [2009] 2 CLC 1004.

36 Council Regulation (EC) No. 44/2001 of 22 December 2001 on ‘jurisdiction and the recognition and enforcement of judgments in civil and commercial matters’.

37 This doctrine precludes the re-opening, in fresh litigation or arbitration between the same parties, of matters decided in earlier litigation, including earlier decisions of foreign courts or the ECJ: N. Andrews, *Contracts and English Dispute Resolution* (Tokyo, 2010), 18.23.

38 *NB Three Shipping Ltd v. Harebell Shipping Ltd* [2004] EWHC 2001 (Comm); [2005] 1 Lloyd’s Rep 509, Morison J; *Law Debenture Trust Corporation plc v. Elektrim Finance BV* [2005] EWHC 1412 (Ch); [2005] 2 Lloyd’s Rep 755, Mann J; S. Nesbitt and H. Quinlan, (2006) 22 *Arbitration International* 133; D. Joseph, *Jurisdiction and Arbitration Agreements and their Enforcement* (London, 2005), 4–29.

39 [2009] EWHC 2097 (Comm).

40 [2008] EWHC 2855 (Comm); [2009] 1 Lloyd’s Rep 167.

Chapter contents

1. Introduction *para.* 13.01
2. Terms implied in law *para.* 13.03
3. Terms implied in fact *para.* 13.08
4. Implied terms: custom or trade usage *para.* 13.16
5. Implied terms and the tort of negligence *para.* 13.19
6. Implied terms and good faith *para.* 13.22
7. Implied terms and the doctrines of mistake and frustration *para.* 13.26

13

Implied terms

1. INTRODUCTION¹

13.01 Summary of main points

- (1) There are three types of implied term:² (i) those implied by law (that is, by statute or by judicial decision); (ii) those implied in fact; and (iii) those implied on the basis of custom or trade usage (see 13.03, 13.08, 13.16 below, respectively). Lord Wright gave a convenient overview of the topic in *Luxor (Eastbourne) Ltd v. Cooper* (1941):³

[Terms implied in law]

The expression 'implied term' is used in different senses. Sometimes it denotes some term which does not depend on the actual intention of the parties but on a rule of law, such as the terms, warranties or conditions which, if not expressly excluded, the law imports, as for instance under the Sale of Goods Act and the Marine Insurance Act.

[Terms implied in fact]

[The] presumption is against the adding to contracts of terms which the parties have not expressed ... But it is well recognised that there may be cases where obviously some term must be implied if the intention of the parties is not to be defeated, some term of which it can be predicated that 'it goes without saying',

1 A. Phang, [1990] JBL 394, [1993] JBL 242, [1994] JBL 255, [1998] JBL 1; E. Peden, (2001) 117 LQR 459–76; T. Rakoff, in J. Beatson and D. Friedmann (eds.), *Good Faith and Fault in Contract Law* (Oxford, 1995), 191 (mostly from a US perspective); C. A. Riley, (2000) 20 OJLS 367–90; R. Goode, (1997) 46 ICLQ 1.

2 On the many types of implied terms, see the reviews in *Bank of Nova Scotia v. Hellenic Mutual War Risks ('The Good Luck')* [1989] 3 All ER 628, 665–8, CA, and in *Philips Electronique Grand Publique SA v. British Sky Broadcasting Ltd* [1995] EMLR 472, CA: on the latter case, see 13.14.

3 [1941] AC 108, 137–8, HL.

some term not expressed but necessary to give to the transaction such business efficacy as the parties must have intended. This does not mean that the Court can embark on a reconstruction of the agreement on equitable principles, or on a view of what the parties should, in the opinion of the Court, reasonably have contemplated. The implication must arise inevitably to give effect to the intention of the parties.

[Need for restraint]

These general observations do little more than warn judges that they have no right to make contracts for the parties. Their province is to interpret contracts. But language is imperfect and there may be, as it were, obvious interstices in what is expressed which have to be filled up.

- (2) A term implied in law can arise under statute, for example, certain provisions of the Sale of Goods Act 1979.
- (3) Judicial precedent is another source of terms implied in law: the High Court or higher courts, in exercise of their common law power to pronounce binding decisions, can find such an implied term. It is now admitted (13.03, 13.04) that judicially prescribed terms implied *in law* will reflect policy considerations and matters of general exigency. A term implied in law by the courts is designed to reflect the essential incidents of well-established transactions.
- (4) The courts are more circumspect in finding a term to be *implied in fact*. This category of implication involves imputing to the parties a readily acknowledged tacit understanding. For this purpose, the so-called 'officious bystander' or 'no need to mention' test is the favoured divining rod (MacKinnon LJ formulated the 'officious bystander' test in *Shirlaw v. Southern Foundries (1926) Ltd* (1939): see 13.10).⁴ An older and vaguer criterion is the 'business efficacy' test, the so-called '*Moorcock* test' (1889) (13.09):⁵ without the suggested term, the contract would not make any real business sense. But this approach can become unruly, for it might be misapplied as a pretext or licence to create a term to which the parties had not implicitly agreed, and to which they would never jointly have assented. Lord Hoffmann, in the Privy Council in *Attorney-General for Belize v. Belize Telecom Ltd* (2009),⁶ criticised both the 'officious bystander' test and the 'necessary for business efficacy' test. Further, he suggested

4 [1939] 2 KB 206, 227–8, CA (affirmed [1940] AC 701, HL).

5 (1889) 14 PD 64, 68, CA; A. Phang, [1998] JBL 1.

6 [2009] UKPC 10; [2009] 2 All ER 1127; [2009] BCC 433, at [16] to [27].

that a better test for finding an implied term of fact in a *written contract* is this: the contract should be construed in the manner in which it would be understood by its reasonable addressee, so as to give effect to the overall purpose of the document, but eschewing judicial discovery of implied terms of fact on the basis of reasonableness. But it is doubtful whether Lord Hoffmann's remarks will prove helpful: see 13.15, sub-paragraph (5).

- (5) For a term to be implied on the basis of custom or trade usage, the suggested term must be very clearly supported by settled practice.
- (6) The technique of implying terms on any of the three bases mentioned at (1) above – law, fact, or custom – allows the courts (and the legislature in the case of terms *implied in law*) to do justice in either a generous or circumspect fashion, depending on the context. The English method of 'implying terms' under these various rubrics largely explains the absence of an express general principle of commercial 'good faith' in the performance of contracts (see 13.22; and generally on the 'good faith' issue, see 21.03).
- (7) Both the (ostensibly) cautious approach in English law to the implication of terms and the distinction drawn between (judicially recognised) terms implied in law and terms implied in fact are to be contrasted with the more open-textured criteria espoused in the (non-binding) codes, PECL, *Principles of European Contract Law*,⁷ the Common Frame of Reference,⁸ and UNIDROIT's *Principles of International Commercial Contracts* (2004).⁹ These 'soft law' codes refer to 'good faith and fair dealing', and the UNIDROIT Principles includes 'reasonableness' as a factor. These soft law codes also contain an explicit general requirement that each party must co-operate to perform and fulfil the contract¹⁰ (generally on the 'good faith' issue, see 21.03).
- (8) Under English law, there will often be overlapping liability in the tort of negligence and in contract, based on an implied term that the defendant must exercise reasonable care or display customary skill (13.19).

7 Article 6:102 of PECL.

8 UNIDROIT, Article III-1:103 of the *Principles, Definitions and Model Rules of European Private Law Draft Common Frame of Reference*, ed. Christian von Bar and Eric Clive (6 vols., Oxford University Press/Sellier, 2010), prepared by the 'Study Group on a European Civil Code' and the 'Research Group on EC Private Law (Acquis Group)'.

9 Article 5.1.2; on the UNIDROIT Principles, see M. J. Bonell (ed.), *The UNIDROIT Principles in Practice: Case Law and Bibliography on the UNIDROIT Principles of International Commercial Contracts* (2nd edn, Ardsley, NY, 2006), 246–8, 251–4; S. Vogenauer and J. Kleinheisterkamp (eds.), *Commentary on the UNIDROIT Principles of International Commercial Contracts* (Oxford, 2009), 534 ff, 541 ff.

10 PECL, Article 1:102, and UNIDROIT, Articles 4.8, 5.1.3.

Terms judicially implied in law

E. Peden, 'Policy Concerns Behind Implication of Terms in Law' (2001) 117 LQR 459–76, especially 467 ff

Terms implied in fact

A. Phang, 'Implied Terms, Business Efficacy and the Officious Bystander – A Modern History' [1998] JBL 1 (see also other articles by Phang at [1990] JBL 394; [1993] JBL 242; and [1994] JBL 255)

Wider perspective of commercial reasonableness

Lord Steyn, 'Contract Law: Fulfilling the Reasonable Expectations of Honest Men' (1997) 113 LQR 433, 442

- 13.02 Implied terms (especially those implied by law (13.03)) are more common than express terms. Every day, millions of transactions are entered into without writing, and without a single spoken word, for English shopkeepers and consumers respect each other's human right to remain mute. Against this silent background, the law fleshes out these transactions by implying terms, notably terms implied in law.

2. TERMS IMPLIED IN LAW

- 13.03 As Lord Steyn in *Equitable Life Assurance Co. Ltd v. Hyman* (2002) explained, terms implied in law are 'incidents impliedly annexed to particular forms of contracts ... Such standardised implied terms operate as general default rules.'¹¹ Implied terms in law are often the product of legislation governing particular standard contracts. The Sale of Goods Act 1979¹² (earlier the Act of 1893)¹³ and the Supply of Goods and Services Act 1982 are the best examples. As for judicially recognised implied terms in law, the House of Lords admitted that general considerations of policy underpin decisions whether to add to this canon of terms implied in law.¹⁴ Elizabeth Peden has identified a wide array of factors in the modern cases.¹⁵ But, when implying a term

11 [2002] 1 AC 408, 458–9 HL; comments of Lord Somervell in *Lister v. Romford Ice & Cold Storage Co.* [1957] AC 555, 598, HL; for overt gap-filling and explicit reference to fairness, in the context of credit card payments, see *Re Charge Card Services Ltd* [1989] Ch 497, 513, CA.

12 Section 12 of the Sale of Goods Act 1979 (implied term that seller should have good title to the goods; *ibid.*, section 13 (implied term that goods correspond to any description made or accepted by the vendor; *ibid.*, section 14(2) (implied term that goods are of satisfactory quality; *ibid.*, section 14(3) (implied term that goods are reasonably fit for their purpose); *ibid.*, section 15 (sales by sample; implied term that goods correspond to sampled goods); see *Anson's Law of Contract* (29th edn, Oxford, 2010), 159 ff.

13 On the 1893 Act's implied terms in this perspective, see Lord Somervell in *Lister v. Romford Ice & Cold Storage Co.* [1957] AC 555, 598, HL.

14 Lord Wright in *Luxor (Eastbourne) Ltd v. Cooper* [1941] AC 108, 137, HL (cited at 13.01); Viscount Simonds and Lord Tucker in *Lister v. Romford Ice & Cold Storage Co.* [1957] AC 555, 576, 594, HL.

15 E. Peden, 'Policy Concerns Behind Implication of Terms in Law' (2001) LQR 459–76.

in law, the overall consideration is the court's perception of what is 'reasonable' in transactions of a common type.¹⁶

13.04 *Local authority duty to 'high-rise' flats tenants.* In *Liverpool City Council v. Irwin* (1977), the issue was whether an implied term in law should be recognised to govern the so-called 'common parts' of local authority 'high-rise' flats (an important, but often unsatisfactory, type of housing in modern Britain).¹⁷ The tenants had complained that the local authority had failed to maintain the stairways and lifts. Many of the tenants were either elderly or parents of young children. The House of Lords held that the landlord should exercise reasonable care to keep the common parts in reasonable repair. Such a term should be implied as a matter of law (although, on the facts, it was held that the obligation had not been breached). Although the speeches contain various formulations of the general test for finding an implied term in law, the gist is that the court here found *an obligation essential to the relations between a landlord and tenants inhabiting a block of flats*. This is encapsulated in Lord Salmon's statement:¹⁸

I find it difficult to think of any term which it could be more necessary to imply than one without which the whole transaction would become futile, inefficacious and absurd as it would do if in a 15 storey block of flats or maisonettes, such as the present, the landlords were under no legal duty to take reasonable care to keep the lifts in working order and the staircases lit.

Although this decision suggests that even a term 'implied in law' will only be found where it is clearly required or necessary,¹⁹ more recently the Court of Appeal in the *Crossley* case (2004) admitted that the concept of 'necessity' is 'somewhat protean'²⁰ and that the 'existence and scope of standardised implied terms [that is, those implied in law] raise questions of reasonableness, fairness and the balancing of competing policy considerations'.²¹ Dyson LJ in this case approved the following passage in *Anson's Law of Contract* (2002):²²

In these cases concerning a common relationship, for example sale, carriage, landlord and tenant, or employment, the parties may have left a lot unsaid and the process of implication is different. It involves the court determining, in light of general considerations of policy, the standard incidents of the particular type of relationship rather than constructing a hypothetical bargain. Although it has sometimes been said that the criterion for this form of implication is also 'necessity' rather than 'reasonableness', it does appear that a broader approach is taken.

¹⁶ Lord Steyn, 'Contract Law: Fulfilling the Reasonable Expectations of Honest Men' (1997) 113 LQR 433, 442.

¹⁷ [1977] AC 239, HL.

¹⁸ [1977] AC 239, 263, HL; cited by Lord Scarman in *Tai Hing Cotton Mill Ltd v. Liu Chong Hing Bank Ltd* [1986] AC 80, 105, PC and by Peter Coulson QC (sitting as a judge of the High Court) in *Jani-King (GB) Ltd v. Pula Enterprises Ltd* [2007] EWHC 2433 (QBD); [2008] 1 Lloyd's Rep 305, at [47].

¹⁹ *Liverpool City Council v. Irwin* [1977] AC 239, 254, 257–8, 266, HL.

²⁰ *Crossley v. Faithful & Gould Holdings Ltd* [2004] ICR 1615, CA, at [34], *per* Dyson LJ.

²¹ *Ibid.*, at [36].

²² *Ibid.*, at [30], quoting from *Anson's Law of Contract*.

13.05 Arbitration. In *Michael Wilson & Partners Ltd v. Emmott* (2008), the Court of Appeal acknowledged that an obligation of confidentiality arises as a matter of law in arbitration references conducted in accordance with English law²³ (for earlier recognition of this implied term of law, see *Ali Shipping Corporation v. Shipyard Trogir* (1999)).²⁴ This implied term governs all documents ‘prepared for’, ‘used’ and ‘disclosed during’ such arbitration. In the *Michael Wilson* case (2008), Lawrence Collins LJ commented:²⁵ ‘This is in reality a substantive rule of arbitration law reached through the device of an implied term’ (this comment echoes Lord Wright’s observation on the nature of implied terms in law, in *Luxor (Eastbourne) Ltd v. Cooper* (1941),²⁶ cited at 13.01). The English courts recognise various exceptional contexts in which arbitral confidentiality will not prevail. Lawrence Collins LJ summarised the position as follows:²⁷

[T]he principal cases in which disclosure will be permissible are these: the first is where there is consent, express or implied; second, where there is an order, or leave of the court (but that does not mean that the court has a general discretion to lift the obligation of confidentiality); third, where it is reasonably necessary for the protection of the legitimate interests of an arbitrating party;²⁸ fourth, where the interests of justice require disclosure, and also (perhaps) where the public interest requires disclosure.

13.06 Holiday injury: tour operator’s contractual duty of care. Both at common law and under a statutory provision,²⁹ a tour operator is contractually required to take reasonable steps to guard against personal injury. However, in *Evans v. Kosmar Villa Operators* (2008),³⁰ the Court of Appeal held that this duty did not require the operator to protect a 17-year-old against the danger of injury caused by diving into the shallow end of a swimming pool. The court took the view that the claimant was aware of the danger, for he had spent enough time at the hotel to have appreciated this risk; but he had momentarily forgotten it, or decided to run this risk; he was not a child; it would have made no difference if the tour operators had provided more prominent signage warning against the danger. The decision does not, however, convincingly address the fact that the defendant had acquiesced in the practice of diving into this pool. There was no evidence that the defendant had taken active steps to stamp out the practice of ‘copycat diving’. A more exacting duty, as found by the trial judge, seems appropriate. The Court of Appeal’s decision is harsh.

13.07 Employment cases. This has been a fertile context for the implication of terms in law. In the *ASLEF* case (1972), the Court of Appeal implied a term that employees will not act so as to prevent effective performance of their duties and of their employers’

23 [2008] EWCA Civ 184; [2008] Bus LR 1361; [2008] 1 Lloyd’s Rep 616.

24 [1999] 1 WLR 314, CA.

25 [2008] EWCA Civ 184; [2008] Bus LR 1361; [2008] 1 Lloyd’s Rep 616, at [105] and [106].

26 [1941] AC 108, 137–8, HL.

27 [2008] EWCA Civ 184; [2008] Bus LR 1361; [2008] 1 Lloyd’s Rep 616, at [107].

28 *Ibid.*, at [101].

29 Package Travel, Package Holidays and Package Tours Regulations 1992 (SI 1992 No. 3288), reg. 15.

30 [2007] EWCA Civ 1003; [2008] 1 WLR 297.

enterprise.³¹ In this case, railway employees had pedantically stuck to the very letter of their contract in order to produce industrial chaos (so-called 'working to rule'). With feigned zeal, they had carefully checked each carriage door before allowing passenger trains to leave the platform. This had caused chaotic delay. Buckley and Roskill LJ implied a term that employees would not wreck their employer's commercial venture. Since this 1972 decision, however, most of the decisions have been successes on the employee side (although contrast the *Crossley* case, discussed below). As the following four decisions show, the courts have been willing to mould the employment contract, using the implied term device, to impose various additional obligations upon employers.³²

- (1) *Overworking the young. Johnstone v. Bloomsbury Health Authority* (1992) (see also 13.19) concerned junior doctors' working hours within the National Health Service.³³ The Court of Appeal affirmed that there is an implied term that a health employer will not overwork its staff so that their health is harmed. This tortious duty of care overlaps with an identical contractual implied term (in law): 'the two duties run side by side'.³⁴ The Court of Appeal wrestled with the problem of reconciling this implied duty with an express term of the employment contract, which allowed the employer to require these doctors to work extensive overtime. The majority held that this power to extend the working week (by forty-eight hours on top of the basic forty hours) should be read as subject to the implied term which requires the employer to safeguard the employee against injury or illness.³⁵
- (2) Crooked management damaging the future prospects of innocent employees. The House of Lords in *Malik (and Mahmud) v. Bank of Credit and Commerce International SA* (1998) recognised a general implied term that the employer should not behave in a way which will destroy or threaten the relationship of confidence and trust between him and his employees.³⁶

The employer in the last case was a bank. Its senior officers had been dealing dishonestly. As a result the bank became insolvent. The liquidator terminated the plaintiffs' employment contracts. The House of Lords recognised that there is an implied term in law that an employer will not act dishonestly, because such misconduct will taint innocent employees. Because of the 'stigma' of their association with the dishonest bank, they might find it hard to gain new and equivalent employment. Although the House of Lords created this new employee's right to seek compensation, in the next stage of the litigation, the claim for 'stigma' damages failed on

31 *Secretary of State for Employment v. ASLEF (No. 2)* [1972] 2 QB 455, CA.

32 See the statements of high authority on the general background to this judicial activism: *Crossley v. Faithful & Gould Holdings Ltd* [2004] ICR 1615, CA, at [36] to [42]; for a study of implied terms in this context, see R. Rideout, in R. Halson (ed.), *Exploring the Boundaries of Contract* (Aldershot, 1996), chapter 7.

33 [1992] 1 QB 333, CA; noted by A. Weir, [1991] CLJ 397.

34 [1992] 1 QB 333, 343D, CA, per Stuart-Smith LJ.

35 *Ibid.*, at 344F, per Stuart-Smith LJ; 350–1, per Sir Nicolas Browne-Wilkinson (express power to require up to forty-eight extra hours, to be construed as subject to the implied term not to injure the claimant); Leggatt LJ dissented at 348.

36 [1998] 1 AC 20, 45–6, HL, per Lord Steyn.

the facts, because the employees could not show that they had in fact suffered loss through the stigma of this association.³⁷

- (3) *Assistance in avoiding a pensions snare.* In *Scally v. Southern Health Board* (1992),³⁸ the House of Lords held that an employer was obliged to bring to an employee's attention certain pension technicalities. Such information would enable the employee to 'buy' extra pensionable 'years' and so enhance his eventual pension. The basis was not an implied term in fact,³⁹ but a term implied in law 'based on wider considerations' and in recognition of a 'necessary incident of a definable category of contractual relationship'.⁴⁰ Lord Bridge formulated this implied term with considerable precision as follows:⁴¹

I would define it as the relationship of employer and employee where the following circumstances obtain: (1) the terms of the contract of employment have not been negotiated with the individual employee but result from negotiation with a representative body or are otherwise incorporated by reference; (2) a particular term of the contract makes available to the employee a valuable right contingent upon action being taken by him to avail himself of its benefit; (3) the employee cannot, in all the circumstances, reasonably be expected to be aware of the term unless it is drawn to his attention. I fully appreciate that the criterion to justify an implication of this kind is necessity, not reasonableness. But I take the view that it is not merely reasonable, but necessary, in the circumstances postulated, to imply an obligation on the employer to take reasonable steps to bring the term of the contract in question to the employee's attention, so that he may be in a position to enjoy its benefit. Accordingly I would hold that there was an implied term in each of the plaintiffs' contracts of employment of which the boards were in each case in breach.

The *Scally* case was described at first instance in the *Crossley* case (see below) as 'a bridgehead from which there has been no advance'.⁴² It would appear that the striking feature of the *Scally* case's facts was that employees could not 'reasonably be expected to be aware' of this valuable benefit, unless the employer brought it to their attention. Finally on this case, some commentators have

37 The 'factual sequel': *Bank of Credit & Commerce International SA (in liquidation) v. Ali (No. 2)* [2002] EWCA Civ 82; [2002] 3 All ER 750; [2002] ICR 1258.

38 [1992] 1 AC 294, 306G–307E, HL (noted by M. Freedland, (1992) 21 ILJ 135); distinguished in *University of Nottingham v. Eyett* [1999] 2 All ER 437, 443G–444; [1999] ICR 721, Hart J; *National Home Loans Corporation v. Giffen & Archer* [1997] 3 All ER 808, 814–16, CA; *Oughtram v. Academy Plastics* [2001] ICR 367, CA; *Hagen v. ICI Chemicals & Polymers Ltd* [2002] IRLR 31, Elias J; cases reviewed in *Crossley v. Faithful & Gould Holdings Ltd* [2004] ICR 1615, CA; cf also, no duty upon bank to inform customer of new type of account: *Suriya & Douglas v. Midland Bank*, *The Times*, 29 March 1999, CA.

39 [1992] 1 AC 294, 306G.

40 *Ibid.*, at 307.

41 *Ibid.*

42 [2004] ICR 1615, CA, at [20], *per* Judge Peter Langan QC, cited by Dyson LJ.

suggested that the *Scally* case renders the ‘implied in law or in fact’ distinction ‘fragile’.⁴³ This criticism is unconvincing. Lord Bridge’s very precise formulation – just set out – seems apt when one considers the multiplicity of employment relationships and the variety of possible issues.

- (4) *No duty to provide more detailed pensions advice*. The Court of Appeal in *Crossley v. Faithful & Gould Holdings Ltd* (2004)⁴⁴ noted that cases subsequent⁴⁵ to the *Scally* case had proceeded very cautiously. The Court of Appeal endorsed this circumspect approach and refused to impose a general implied term in law that employers should exercise care to protect their employees’ financial well-being. In the *Crossley* case, the claimant was a senior employee who had taken retirement without proper regard for his pension rights. It was held that he had no cause of action against his employer for failing to provide him with precise guidance so as to maximise his pension-related rights. Dyson LJ said that it would be ‘unfair and unreasonable’ to impose upon employers a general or demanding duty to provide financial advice.⁴⁶ The employee can seek his own advice, and the employer might have a conflict of interests.⁴⁷

3. TERMS IMPLIED IN FACT

- 13.08 *A stricter approach*. We have seen in the preceding section that the criteria for finding a term implied *in law* are relatively free-ranging because that type of regulation requires the courts, in the absence of statutory intervention, to fashion minimal rules for the operation of standard legal relationships. The courts are not then tied to a single criterion of the parties’ tacit joint intention. By contrast, the courts will not find an implied term *in fact* merely because it would be ‘reasonable’ or ‘fair’. Instead, here the courts are endeavouring to tease out the parties’ unexpressed common intention. As Lord Wright said in the *Luxor* case (1941) of this type of implied term: ‘[The courts will not] embark on a reconstruction of the agreement on equitable principles, or on a view of what the parties should, in the opinion of the Court, reasonably have contemplated ... Judges ... have no right to make contracts for the parties.’⁴⁸

- 13.09 *‘Business efficacy’ test: genesis*. This test emerged in Bowen LJ’s judgment in *‘The Moorcock’* (1889):⁴⁹

In business transactions such as this, what the law desires to effect by the implication is to give such business efficacy to the transaction as must have been intended at all events

43 *Anson’s Law of Contract* (29th edn, Oxford, 2010), 156–7; A. Phang, [1993] JBL 242, and [1994] JBL 255.

44 [2004] ICR 1615, CA.

45 *University of Nottingham v. Eyett* [1999] 2 All ER 437, 443G–444; [1999] ICR 721, Hart J; *Oughtram v. Academy Plastics* [2001] ICR 367, CA; *Hagen v. ICI Chemicals & Polymers Ltd* [2002] IRLR 31, Elias J.

46 [2004] ICR 1615, CA, at [43].

47 *Ibid.*, at [44].

48 *Luxor (Eastbourne) Ltd v. Cooper* [1941] AC 108, 137, HL.

49 (1889) 14 PD 64, 68, CA; A. Phang, [1998] JBL 1.

by both parties who are businessmen; not to impose on one side all the perils of the transaction, or to emancipate one side from all the chances of failure, but to make each party promise in law as much, at all events, as it must have been in the contemplation of both parties that he should be responsible for in respect of those perils or chances.

The facts and decision in '*The Moorcock*' case are as follows.

The claimants had moored their boat at the defendant's wharf on the River Thames. Unknown to the claimant, at low tides there was a mound in the river (which did not evenly support the whole vessel). This rendered the berth unsafe. The claimant's vessel was damaged when it came to rest on that mound. The Court of Appeal held that the contract (under which the claimant would pay for use of the defendant's cranes, but not for the mooring itself) imported an implied term that the defendant would take reasonable steps to guard against or point out physical hazards not known to the claimant. Unless that implied term were found, the claimant would be entering into a contract which was effectively a nonsense: for he would be taking the risk of the vessel being severely damaged, even though the defendant had accumulated a vast knowledge of the wharf's characteristics. It was not difficult to apply the 'business efficacy' test to the facts of '*The Moorcock*' (1889), for the defendant's commercial gain from crane charges could only be 'honestly' (the word used by Lord Esher MR) earned if the defendant took minimal legal responsibility to point out the hazard lurking beneath the water.

The business efficacy test can be illustrated by the following examples:

- (1) The test did not avail the claimant in *Easton v. Hitchcock* (1912).⁵⁰ The claimant, a female private detective, was hired by the defendant, a married woman, to watch the latter's husband from January to April 1911. The claimant delegated this task to various men, including, in January, Davis. Davis then ceased to work for the claimant. On 21 February, Davis, acting either spitefully or perhaps for money, 'leaked' to the defendant's husband the fact that a secret watch was being kept. When the defendant discovered this, she refused to pay for the plaintiff's services from 21 February, contending that the service was useless from that date. The question was whether a former employee's decision to scupper the secret arrangement was imputable to the claimant on the basis of 'business efficacy'. The Divisional Court, Hamilton and Lush JJ, held that no implied term arose that a former employee would not divulge a secret. Hamilton J said:⁵¹

I think it impossible to hold that the plaintiff warranted that her servants would not make improper disclosures after they had ceased to be in her employment ... If the warranty is ... to continue for a week it must equally hold good during the whole of the departed servant's life ... The rule is that in all cases of implied warranty 'the law is raising an implication from the

⁵⁰ [1912] 1 KB 535, Divisional Court.

⁵¹ *Ibid.*, at 537–8, Divisional Court.

presumed intention of the parties with the object of giving to the transaction such efficacy as both parties must have intended that at all events it should have': *per* Bowen LJ, '*The Moorcock*'. If a person who employs an agent of this description wishes to protect himself against breaches of confidence by the agent's servants he should expressly stipulate in the contract to that effect.

- (2) Nor, as Blair J held in the *Strydom* case (2009),⁵² was it necessary from the perspective of business efficacy to imply a term into a conditional fee agreement that the solicitor should disclose to his client that the solicitor would receive a fee not just from the claimant but from a government agency (in connection with claims arising from 'White Finger' syndrome).
- (3) But the test was successfully invoked by claimants in *Silverman v. Imperial London Hotels Ltd* (1927).⁵³ They had spent a relatively cheap, but ultimately itchy, night at the defendant's London hotel. With the management's permission, they had slept on couches within a Turkish bath. However, they had unwittingly shared these couches with insects, for the couches were infested with bugs and these had bitten the claimants. Swift J, awarding damages for breach of an implied term in fact, said:

Applying [*'The Moorcock'* test] ... the parties in this case contemplated that the cubicle and ... couch ... should be free from bugs or other insects which might inflict harm upon the plaintiff, and ... there was implied a term that the premises should be so free from bugs as to be reasonably fit for the purpose for which they were to be used ... [It] matters nothing what steps the defendants had taken to render their premises fit ... It avails the defendants nothing although they have taken every possible step in an endeavour to make them fit.

The 'business efficacy' test is therefore pliable: either it can be used restrictively to permit a term to be recognised only if its absence would render the contract a waste of time and an absurdly uncommercial venture (this was the narrow focus of the judgments in '*The Moorcock*' (1889) itself: see above); or it can be used to reflect a broader range of factors supporting inclusion of a particular term. Indeed, Bowen LJ's *ex tempore* judgment in 1889, read as a whole, is less than crystal clear, and ranges quite broadly.⁵⁴ For this reason, MacKinnon LJ in the *Shirlaw* case (1939)⁵⁵ (on which see 13.10 below) was critical of the nineteenth-century test in '*The Moorcock*':

I recognise that the right or duty of a Court to find the existence of an implied term or implied terms in a written contract is a matter to be exercised with care; and a Court is too often invited to do so upon vague and uncertain grounds. Too often also such an invitation is backed by the citation of a sentence or two from the judgment of Bowen LJ in '*The Moorcock*'. They are sentences from an *extempore* judgment as

⁵² *Strydom v. Vendside Ltd* [2009] EWHC 2130 (QB); [2009] 6 Costs LR 886, at [28] to [33].

⁵³ [1927] All ER 712, 714; 137 LT 57; 43 TLR 260.

⁵⁴ As observed by MacKinnon LJ in *Shirlaw v. Southern Foundries (1926) Ltd* [1939] 2 KB 206, 227, CA (affirmed [1940] AC 701, HL).

⁵⁵ *Ibid.*

sound and sensible as all the utterances of that great judge; but I fancy that he would have been rather surprised if he could have foreseen that these general remarks of his would come to be a favourite citation of a supposed principle of law, and I even think that he might sympathise with the occasional impatience of his successors when '*The Moorcock*' is so often flushed for them in that guise.

- 13.10 '*Officious bystander test*'. The main criterion adopted by the courts for the finding of a term implied *in fact* is the 'officious bystander' test. The test amounts to this: whether, following the intervention of a kindly and imaginary pedant habitually given to stalking negotiating parties, the prospective contractual parties would have readily assented to the proposed term at the time of formation. The test emphasises the need for 'obviousness': and this demanding criterion prevents an implied term from being recognised if one party would never, or only doubtfully, have assented to it. The 'objective bystander' test establishes a very high threshold: a term will not be recognised if one of the parties can plausibly protest that, if the matter had been explicitly raised during negotiation, he would never, or only doubtfully, have assented to it. The attraction of this approach is that it does not conflict with the principle of freedom of contract (1.08), that is, respect for the parties' general liberty to fix their own terms. MacKinnon LJ formulated the 'officious bystander' test in *Shirlaw v. Southern Foundries (1926) Ltd* (1939) as follows:⁵⁶

If I may quote from an essay which I wrote some years ago, I then said: 'Prima facie that which in any contract is left to be implied and need not be expressed is something so obvious that it goes without saying; so that, if, while the parties were making their bargain, an officious bystander were to suggest some express provision for it in their agreement, they would testily suppress him with a common "Oh, of course!" At least it is true, I think, that, if a term were never implied by a judge unless it could pass that test, he could not be held to be wrong.'

In fact, this test is clearly derived from Scrutton LJ's statement in *Reigate v. Union Manufacturing Co. (Ramsbottom) Ltd* (1918) (Scrutton had been MacKinnon's pupil-master at the Bar):⁵⁷

A term can only be implied if it is necessary in the business sense to give efficacy to the contract; that is, if it is such a term that it can confidently be said that if at the time the contract was being negotiated some one had said to the parties, 'What will happen in such a case', they would both have replied, 'Of course, so and so will happen; we did not trouble to say that; it is too clear.'

MacKinnon LJ's statement has become the leading decision on terms *implied in fact*, much cited in modern cases. Indeed, Treitel says:⁵⁸ '[M]ost of the authorities ... are based on the assumption that a term cannot be implied in fact where the evidence actually negatives

⁵⁶ *Ibid.*

⁵⁷ [1918] 1 KB 592, 605, CA.

⁵⁸ *Treitel* (12th edn, London, 2007), 6-031.

the “officious bystander” test.’ In other words, the officious bystander test trumps the test in *The Moorcock* (1889) (13.09): if a putative term which is supported by the ‘business efficacy’ test does not also satisfy the ‘officious bystander’ test, the courts will refuse to recognise it as a term to be implied in fact. The ‘business efficacy’ test is no more than a pointer, not itself conclusive, towards the establishment of a tacit term which is so ‘obvious’ that it reflects the parties’ unspoken shared intention. Sometimes, the concept of ‘business efficacy’ has been merged, even in the same passage or sentence, with the ‘officious bystander’ test, as the following cases illustrate.⁵⁹

In *Reigate v. Union Manufacturing Co. (Ramsbottom) Ltd* (1918), Scrutton LJ said:

A term can only be implied if it is necessary in the business sense to give efficacy to the contract; that is if it is such a term that it can confidently be said that if at the time the contract was being negotiated someone had said to the parties, ‘What will happen in such a case?’, they would both have replied: ‘Of course, so and so will happen; we did not bother to say that; it is too clear.’⁶⁰

Similar formulations were adopted by Lord Wright in the House of Lords in *Luxor (Eastbourne) Ltd v. Cooper* (1941).⁶¹

In *BP Refinery (Westernport) Pty Ltd v. Shire of Hastings* (1978), Lord Simon, giving the Privy Council’s judgment, said that the ‘business efficacy’ and ‘officious bystander’ tests are both means of eliciting the parties’ common intention (His Lordship must be taken to have been referring to the category of terms implied in fact rather than in law),⁶² and that the ‘business efficacy’ test is not a sufficient criterion.⁶³ The Privy Council in that case said that the court’s decision whether to recognise an implied term in fact will be regulated by the following factors:⁶⁴

... (which may overlap) ... (1) it must be reasonable and equitable; (2) it must be necessary to give business efficacy to the contract, so that no term will be implied if the contract is effective without it; (3) it must be so obvious that ‘it goes without saying’; (4) it must be capable of clear expression;⁶⁵ (5) it must not contradict any express term of the contract.⁶⁶

59 [2008] EWHC 1420 (TCC); [2008] BLR 436, at [10] (Frances Kirkham, sitting as a Deputy High Court Judge).

60 [1918] 1 KB 592, 605, CA.

61 [1941] AC 108, 137, HL.

62 (1978) 52 ALJR 20, PC; cited by Bingham LJ in *Philips Electronique Grand Publique SA v. British Sky Broadcasting Ltd* [1995] EMLR 472, CA: on this case, 13.14; also cited in the *Attorney-General of Belize* case (2009), PC: see text immediately following.

63 *Ibid.*, at 26, PC.

64 (1978) 52 ALJR 20, 26, PC.

65 A vague and uncertain term is unlikely to be accepted: *Shell v. Lostock* [1977] 1 All ER 481, 491G, CA, per Ormrod LJ; cf Bridge LJ’s dissent, *ibid.*, at 494. For an example of a suggested implied term which could not be satisfactorily formulated, but admitted of several possible variants, see *Luxor (Eastbourne) Ltd v. Cooper* [1941] AC 108, 115–18, HL, Viscount Simon LC concluding at 117: ‘I find it impossible to formulate with adequate precision the tests which should determine whether or not a “just excuse” exists for disregarding the alleged implied term, and this leads me to consider whether there really is any such implied term at all.’

66 *County Homesearch Co. (Thames & Chilterns) Ltd v. Cowham* [2008] EWCA Civ 26, at [19]; [2008] 1 WLR 909.

Commenting on these criteria, Lord Hoffmann said in *Attorney-General for Belize v. Belize Telecom Ltd* (2009) (problematic aspects of his discussion are noted at 13.15):⁶⁷

[T]his list is best regarded, not as a series of independent tests which must each be surmounted, but rather as a collection of different ways in which judges have tried to express the central idea that the proposed implied term must spell out what the contract actually involves.

The following three cases illustrate the officious bystander test.

In *Spring v. National Amalgamated Stevedores and Dockers Society* (1956), the Transport & General Workers' Union (TGWU) dismissed Spring, a Liverpool docker, from their union because he had joined another trade union. The Bridlington Agreement, applicable between trades unions, prohibited each trade union from soliciting membership from each other. The TGWU alleged that, in his contract of membership with the TGWU, the need for a member of the TGWU to comply with the Bridlington Agreement had been incorporated as an implied term in fact. Sir Leonard Stone V-C rejected this:⁶⁸

If the [officious bystander] test were to be applied to the facts of the present case and the bystander had asked the plaintiff at the time he paid his five shillings and signed the acceptance form, 'Won't you put into it some reference to the Bridlington Agreement?', I think (indeed, I have no doubt) the plaintiff would have answered 'What's that?' In my judgment, that is sufficient to dispose of this case.

A more recent example is provided by *R Griggs Group v. Evans (No. 1)* (2005):

In *R Griggs Group v. Evans (No. 1)* (2005), Evans was commissioned to produce a logo for the owners of 'Doc Martens' footwear. Evans contended that he retained worldwide copyright in the logo. Jacob LJ at first instance dismissed the contention that Evans should have that right as a matter of implied terms as 'fantastic':⁶⁹

I find that [contention] fantastic. If an officious bystander had asked at the time of contract whether Mr Evans was going to retain rights in the combined logo which could be used against the client by Mr Evans (or anyone to whom he sold the rights) anywhere in the world, other than in respect of point of sale material in the UK, the answer would surely have been 'of course not'.

Finally, in *Weldon v. GRE Linked Life Assurance Ltd* (2002), Nelson J held that an implied term exists to prevent a company cancelling a life insurance policy after it had itself inefficiently failed to collect payment under a direct debit arrangement.⁷⁰

- 13.11 Contamination of 'policy factors'.** Terms implied in fact must be hard won. The courts should show humility, restraint and respect for the parties' consensual autonomy. However,

67 [2009] UKPC 10; [2009] 2 All ER 1127; [2009] BCC 433, at [27].

68 [1956] 1 WLR 585, 599.

69 [2005] EWCA Civ 11; [2005] FSR 31, at [19].

70 [2000] 2 All ER (Comm) 914, at [19] to [21], Nelson J.

unfortunately, some modern decisions have hinted that the quest for implied terms in fact might become policy-orientated. In *Paragon Finance plc v. Nash* (2002) (13.13), the Court of Appeal even referred to the parties' 'reasonable expectations', as one of the criteria for eliciting an 'implied term in fact', or even as an encapsulation of that search⁷¹ (similarly, see Lord Hoffmann in *Attorney-General for Belize v. Belize Telecom Ltd* (2009): see further 13.15).⁷² The reference to 'reasonable expectations' in the context of *implied in fact* is traceable to a loose passage in Lord Steyn's speech in the *Equitable Life* case (2002) (an ill-starred decision: see 13.12),⁷³ where he said that the relevant term should be implied in fact because it was 'essential to give effect to the reasonable expectations of the parties'. This formulation might conflate the settled distinction between terms implied in fact and terms implied in law (a distinction acknowledged as sound by Lord Steyn writing in the *Law Quarterly Review* in 1997,⁷⁴ where he also made clear that the criterion of 'the reasonable expectations of the parties' might be a convenient test for the implication of terms *in law*, rather than terms implied *in fact*).⁷⁵ It would be most regrettable if 'reasonable expectations' were to become an empty formula apt to mask a more interventionist and prescriptive approach to the implication of terms *in fact*. The concept of 'tacit expectations' (the officious bystander test) is more attractive, because it offers less freedom for the courts to arrogate to themselves, under the pretext of finding tacit intention, the power to impose their own value judgments concerning what would be *reasonable*. Judges are not special jurors selected to recraft transactions in the broad interests of fairness and equity. The appropriate category for a wider-ranging style of 'implication' is terms *implied in law*, a category confined to standard legal relationships. The courts should not loosen the criteria for discovering an implied term in fact by referring to the objective standard of hypothetical parties' 'reasonable expectations'. As Lord Wright said in the *Luxor* case (1941) of this type of implied term: '[The courts will not] embark on a reconstruction of the agreement on equitable principles, or on a view of what the parties should, in the opinion of the Court, reasonably have contemplated ... Judges ... have no right to make contracts for the parties.'⁷⁶

- 13.12 *Financial services cases: a disastrously implied term in fact.* However, the House of Lords erred by inserting an implied term in fact into a complex relationship in *Equitable Life Assurance Co. Ltd v. Hyman* (2002).⁷⁷ The House of Lords considered the predicament of a financially overstretched life insurance and pension company which had proposed to reduce 'final bonus' payments, to the prejudice of one category of policyholders (a group consisting of 90,000 persons). The term 'implied in fact' on complicated commercial facts

71 [2001] EWCA Civ 1466; [2002] 1 WLR 685, at [36] (third sentence), and [42] (second sentence), *per* Dyson LJ.

72 [2009] UKPC 10; [2009] 2 All ER 1127; [2009] BCC 433, at [23].

73 *Equitable Life Assurance Co. Ltd v. Hyman* [2002] 1 AC 408, 459, HL.

74 Lord Steyn, (1997) 113 LQR 432.

75 *Ibid.*, at 442.

76 *Luxor (Eastbourne) Ltd v. Cooper* [1941] AC 108, 137, HL.

77 [2002] 1 AC 408, HL; noted by A. Berg, [2002] JBL 570; on the subsequent litigation against the company's auditors, see L. Roach, (2006) 17 *International Company and Commercial Law Review* 117.

in this case was a long way removed from the commercially transparent context in which MacKinnon LJ in the *Shirlaw* case (1939) (13.10) applied the ‘officious bystander’ test. The decision in the *Equitable Life* case came as a commercial surprise because it ran counter to the emerging practice recognised by the Treasury and other companies (as Morritt LJ, in his dissenting judgment in the Court of Appeal, had noted).⁷⁸

These contracts contained a clause giving the company an ostensibly absolute discretion both whether to grant final bonuses and, if so, how to fix the level of these bonuses. The company had run into difficulty because it had been offering guaranteed annuity rates without making an extra charge. Until October 1993, the guaranteed rate had always been lower than the current annuity rate. But, after May 1995, the guaranteed rate had outstripped the current annuity rate. This had become a major drain on the company. And so the company adopted the new practice of requiring members who were close to retirement to elect whether to opt for the lower current rate, and calculating the final bonus accordingly, or to take a lower final bonus if they instead opted to receive the guaranteed rate.

Scott V-C at first instance (and Morritt LJ in his dissent in the Court of Appeal) had persuasively decided that the contract did not create a right to a final bonus, and that there was no implied term fettering the company’s discretion as to the grant or quantification of these bonuses.

But Lord Woolf MR and Waller LJ in the Court of Appeal, and all five members of the House of Lords, recognised an implied term of fact that would restrain (perceived) misuse of the company’s discretion. The upshot was that the company found itself legally constrained from making a reduced final bonus to the 90,000 disaffected policy-holders (members who, unlike the other members, had contracted – without extra payment – to receive guaranteed annuity rates). In the House of Lords, Lord Steyn said that this ‘individualised’ implied term arose after construction of the entire policy and its context, and that it was founded upon the ‘stringent’ test of ‘strict necessity’.⁷⁹ This was in fact a highly debatable finding of an implied term. The result of the House of Lords decision was that the company almost became insolvent and needed to be commercially rescued.

- 13.13 Lender’s implied term in fact.** A more convincing instance of a term being implied in fact in the commercial context is *Paragon Finance plc v. Nash* (2002).⁸⁰ The Court of Appeal held that there is an implied term that the lender must exercise an express power to vary the rate of interest payable by its customer *without dishonesty, capriciousness or for an improper purpose*.⁸¹ This would prevent the lender from increasing interest to an extent,

⁷⁸ [2002] 1 AC 408, 438–9, at [110], CA, *per* Morritt LJ.

⁷⁹ [2002] 1 AC 408, 459H, *per* Lord Steyn.

⁸⁰ *Paragon Finance plc v. Nash* [2001] EWCA Civ 1466; [2002] 1 WLR 685, at [36] to [42], *per* Dyson LJ, reviewing earlier case law, notably *Gan Insurance Co. Ltd v. Tai Ping Insurance Co. Ltd (No. 2)* [2001] 2 All ER (Comm) 299, CA (noted by V. Sims and R. Goddard, [2002] CLJ 269–71).

⁸¹ *Paragon Finance plc v. Nash* [2001] EWCA Civ 1466; [2002] 1 WLR 685, at [32] and [36].

or in a manner, which no other lender could reasonably make.⁸² The court drew back from stating that the implied term further outlawed any allegedly ‘unreasonable’ exercise of this power.⁸³ Dyson LJ said:⁸⁴

It is one thing to imply a term that a lender will not exercise his discretion in a way that no reasonable lender, acting reasonably, would do. It is unlikely that a lender who was acting in that way would not also be acting either dishonestly, for an improper purpose, capriciously or arbitrarily ... Such an implied term is necessary in order to give effect to the reasonable expectations of the parties.

The Court of Appeal’s decision in *Paragon v. Nash* (2002) involved a transplant into private law of the famous *Wednesbury* principles, well known to students of public law.⁸⁵ These public law principles are used in judicial review proceedings to regulate decisions made by government or other ‘public’ authorities. It is established that a public authority’s decision cannot be judicially impugned unless it was *wholly unreasonable*, that is, a decision that no person could possibly have made; in other words, a perverse or ‘mad-hat’ decision.

Later decisions in the *private law* field indicate that the courts have maintained this narrow criterion of extreme unreasonableness.⁸⁶ This narrow approach is attractive. It satisfies the need for the courts to provide minimal protection of a disadvantaged party. At the same time, this approach is not too ‘interventionist’, because it shields the courts from the charge that they have constructed an entirely new contract for the parties. To overstep that line would be contrary to the principle of freedom of contract (1.08). In that perspective, the result in *Paragon v. Nash* (2002), just considered, reflects the need for ‘minimal judicial intervention’, as envisaged in the seminal case of ‘*The Moorcock*’ (1889), examined at 13.08 above, and as emphasised by Lord Wright in *Luxor (Eastbourne) Ltd v. Cooper* (1941):⁸⁷ ‘Judges ... have no right to make contracts for the parties.’

The restrictive approach in *Paragon v. Nash* just considered is not confined to discretions concerning financial charges. A general principle is discernible. In *Ludgate Insurance Co. Ltd v. Citibank NA* (1998), Brooke LJ said:⁸⁸

It is very well established that the circumstances in which a court will interfere with the exercise by a party to a contract of a contractual discretion given to it by another

82 *Ibid.*, drawing upon *Gan Insurance Co. Ltd v. Tai Ping Insurance Co. Ltd (No. 2)* [2001] 2 All ER (Comm) 299, CA, at [64] to [73], *per* Mance LJ (implied term that reinsurer’s discretion to approve proposed settlement must not be absurdly unreasonable or based on extraneous and non-commercial considerations).

83 *Paragon* case, [2001] EWCA Civ 1466; [2002] 1 WLR 685, at [37] to [42].

84 *Ibid.*, at [41] and [42], *per* Dyson LJ.

85 *Associated Provincial Picture Houses v. Wednesbury Corporation* [1948] 1 KB 223, CA.

86 *Paragon Finance plc v. Plender* [2005] EWCA Civ 760; [2005] 1 WLR 3412, especially at [118] (lender could adopt a policy in pursuit of a genuine commercial reason of tracking other similar commercial rates of interest); *Lymington Marina Ltd v. MacNamara* [2007] EWCA Civ 151; [2007] Bus LR D29 (right to withhold permission for sub-licence not to be exercised on wholly unreasonable, capricious, arbitrary or bad faith reasons).

87 [1941] AC 108, 137–8, HL.

88 [1998] Lloyd’s LR 221, CA, at [35]; followed by Peter Coulson QC (sitting as a High Court judge) in *Jani-King (GB) Ltd v. Pula Enterprises Ltd* [2007] EWHC 2433 (QBD); [2008] 1 Lloyd’s Rep 305, at [34].

party are extremely limited ... Provided the discretion is exercised honestly and in good faith for the purposes for which it was conferred, and provided also that it was a true exercise of discretion in the sense that it was not capricious or arbitrary or so outrageous in its defiance of reason that it can properly be categorised as perverse, the courts will not intervene.

However, it would appear more obvious that the implied term found in *Paragon v. Nash* (2002) might be generalised as an implied term *in law*: after all, the courts are here establishing a framework for a very common type of contract. It is a long way removed from the exotic situations considered in both '*The Moorcock*' (1889) (13.09) (a wharf owner's liability to point out unusual berthing hazard at low tide at its section of the River Thames) and the *Shirlaw* case (1939) (13.10) (company X liable on an implied term if its managing director, P, is dismissed by a roundabout stratagem of company Y acquiring control of company X and securing automatic cessation of P's position).

- 13.14 *Implied terms and complex commercial agreements: the need to tread gingerly.* The Court of Appeal's important decision in *Philips Electronique Grand Publique SA v. British Sky Broadcasting Ltd* (1995)⁸⁹ shows that the courts are wary of implying a term of fact into a detailed contract which represents a 'closely negotiated compromise between ... conflicting objectives'⁹⁰ because it would be perilous to impute a common intention in this context.⁹¹

Philips had agreed with BSB, a satellite television company, to manufacture satellite television receivers. At the time there was considerable competition to establish market leadership in the UK. One year after the contract had been formed, BSB realised that it had lost the race to establish market domination and that its rival, Sky, had emerged victorious. BSB announced that it would merge with Sky. This defeat rendered Philips' equipment useless. Before the merger with Sky, BSB elected not to call upon Philips for satellite receivers. No express term required BSB to do so. Philips succeeded at trial, but failed on appeal, to gain recognition of the following implied term: 'that BSB would not commit any act which would tend to impede or render impossible the marketing of the receivers and/or to render the receivers useless or unmarketable.'

Because the contract was not standard, there was no scope for implying a term as a matter of law. As for the test for finding a term as a matter of fact, applying the 'officious bystander'

89 [1995] EMLR 472, CA; Sir Bernard Rix, 'Lord Bingham's Contributions to Commercial Law', in M. Andenas and D. Fairgrieve (eds.), *Tom Bingham and the Transformation of the Law: A Liber Amicorum* (Oxford, 2009), 675; cited with approval by Rix LJ in *Socimer International Bank Ltd (in liquidation) v. Standard Bank London Ltd (No. 2)* [2008] EWCA Civ 116; [2008] 1 Lloyd's Rep 558, at [105]; and by Sir Anthony Clarke MR in *Mediterranean Salvage & Towage Ltd v. Seamar Trading & Commerce Inc. ('The Reborn')* [2009] EWCA Civ 531; [2009] 2 Lloyd's Rep 639, at [16] and [17] (quoted in 13.15 below).

90 *Ali v. Christian Salvesen* [1997] 1 All ER 721, 726, CA (in the context of a collective agreement governing employment relations).

91 *Ibid.*, at 726–7.

test, there was no basis for finding such a term; nor, applying the slightly vaguer 'business efficacy' test, should the term be recognised. In rejecting this proposed implied term in fact, the Court of Appeal noted:

- (1) BSB had not agreed to purchase Philips' equipment;
- (2) BSB had not assumed the risk that the market in products designed by Philips would collapse;
- (3) all the indications were that the parties would have engaged in tough negotiation if Philips had sought such contractual protection;
- (4) the supposed implied term would have completely fettered BSB's commercial decision-making (including its economic decision to merge with a more successful rival).

The decision is sound. Even if (as the first instance judge evidently thought) Philips had an arguable case that the proposed implied term might be consistent with 'business efficacy' (in the sense that there would be no point in manufacturing receivers for a company which had decided to merge with a rival which used a different type of receiver), it would fly in the face of the 'officious bystander' test to impute to the parties a tacit assent to the proposed term. The 'officious bystander' test trumped the vaguer notion of 'business efficacy'.

13.15 *Much ado about written contracts.* Lord Hoffmann, in *Attorney-General for Belize v. Belize Telecom Ltd* (2009),⁹² in one of his final judicial contributions to contract law, criticised both the 'officious bystander' test and the 'business efficacy' test. He suggested that the true test is how a *written contract* should be construed by its reasonable addressee, so as to give effect to the overall purpose of the document, but eschewing the criterion of implication on the basis of reasonableness. He said:

[I]n every case in which it is said that some provision ought to be implied in an instrument, the question for the court is whether such a provision would spell out in express words what the instrument, read against the relevant background, would reasonably be understood to mean. It will be noticed ... that this question can be reformulated in various ways which a court may find helpful in providing an answer – the implied term must 'go without saying', it must be 'necessary to give business efficacy to the contract' and so on – but these are not in the Board's opinion to be treated as different or additional tests. There is only one question: is that what the instrument, read as a whole against the relevant background, would reasonably be understood to mean?

⁹² [2009] UKPC 10; [2009] 2 All ER 1127; [2009] BCC 433, at [21] (see also [16] to [27]) (noted by K. F. K. Low, (2009) 125 LQR 561; C. Peters, [2009] CLJ 513; Paul S. Davies [2010] LMCLQ 140); earlier, A. Kramer, 'Implication in Fact as an Instance of Contractual Interpretation' [2004] CLJ 384; the *Belize* case has been considered in: *Re Lehman Brothers International (Europe) (in administration)* [2009] EWHC 2545 (Ch); *Sectorguard plc v. Dienne plc* [2009] EWHC 2693 (Ch); *Mediterranean Salvage & Towage Ltd v. Seamar Trading & Commerce Inc. ('The Reborn')* [2009] EWCA Civ 531; [2009] 2 Lloyd's Rep 639; *ENE Kos v. Petroleo Brasileiro SA (Petrobras)* [2009] EWHC 1843 (Comm); *Infection Control Enterprises Ltd v. Virrage Industries Ltd* [2009] EWHC 2602 (QB); *JBW Group Ltd v. Westminster City Council* [2009] EWHC 2697 (QB); *Mount Anvil Group Ltd v. Volans Management Ltd* [2009] EWHC 1934 (Ch); and *NHS Business Services Authority v. Ingram* [2009] EWHC 2486 (Ch).

It is submitted that these remarks, made in a Privy Council case, are unlikely to change the way in which terms are implied in fact (and, fortunately, much of the potential ‘sting’ of this discussion has already been removed by Sir Anthony Clarke MR’s remarks in the *Mediterranean Salvage & Towage Ltd* case, quoted at the end of this paragraph).⁹³ Here, it will be enough to suggest that four points must be borne in mind. First, Lord Hoffmann concedes that terms implied in fact are not found by reference to the test of reasonableness, but by reference to a more demanding criterion of necessity.⁹⁴ Secondly, in his critical remarks concerning the ‘officious bystander’ test,⁹⁵ Lord Hoffmann overlooks the long-standing success of that test. Thirdly, the task of implying terms is not, of course, confined to the process of construing (1) written contracts and so Lord Hoffmann’s emphasis upon the perspective of the reasonable addressee of the relevant document can hardly supply the answer for implication of terms across the other categories of (2) agreements reached by conduct or (3) purely oral agreements or (4) partly oral and partly written contracts. Fourthly, his judgment does not cite the admirably cautious remarks of Sir Thomas Bingham MR in *Philips Electronique Grand Public SA v. British Sky Broadcasting Ltd* (1995) (on that case, see 13.14 above), nor the decision in *Ali v. Christian Salvesen* (1997),⁹⁶ concerning the circumscribed process of implying terms within written contracts: to add a term to a written document in the name of the parties’ implicit business aim is hazardous and should be undertaken with great delicacy. As Bingham MR said in the *Philips* case: ‘[I]t is tempting for the court then to fashion a term which will reflect the merits of the situation as they then appear. Tempting, but wrong.’ The full text of Bingham MR’s statement in the *Philips* case is as follows:⁹⁷

The courts’ usual role in contractual interpretation [of written contracts] is, by resolving ambiguities or reconciling apparent inconsistencies, to attribute the true meaning to the language in which the parties themselves have expressed their contract. The implication of contract terms involves a different and altogether more ambitious undertaking: the interpolation of terms to deal with matters for which, *ex hypothesi*, the parties themselves have made no provision.

It is because the implication of terms is so potentially intrusive that the law imposes strict constraints on the exercise of this extraordinary power ... The question of whether a term should be implied, and if so what, almost inevitably arises after a crisis has been reached in the performance of the contract. So the court comes to the task of implication with the benefit of hindsight, and it is tempting for the court then to fashion a term which will reflect the merits of the situation as they then appear. Tempting, but wrong.’

⁹³ [2009] UKPC 10; [2009] 2 All ER 1127; [2009] BCC 433, at [18].

⁹⁴ *Ibid.*, at [19].

⁹⁵ *Ibid.*, at [25].

⁹⁶ [1997] 1 All ER 721, 726, CA.

⁹⁷ *Philips* case, [1995] EMLR 472, 481, CA, *per* Bingham LJ (adopted by Jacob LJ in *R Griggs v. Evans* (No. 1) [2005] EWCA Civ 11; [2005] FSR 31, at [13], and by Lightman J in *Ray v. Classic FM plc* [1998] FSR 622, 641); for an illustration of the reluctance to find an implied term when the express terms already cover

The *Philips* case (1995) was cited with approval by the Court of Appeal in *Mediterranean Salvage & Towage Ltd v. Seamar Trading & Commerce Inc. ('The Reborn')* (2009).⁹⁸ After examining the leading cases on implied terms, including the recent discussion by Lord Hoffmann in the *Belize* case (see above), Sir Anthony Clarke MR concluded as follows:⁹⁹

The significance of both *Liverpool City Council v. Irwin*¹⁰⁰ and the *Philips Electronique* case¹⁰¹ is that they both stress the importance of the test of necessity. Is the proposed implied term necessary to make the contract work? That seems to me to be an entirely appropriate question to ask in considering whether a term should be implied on the assumed facts in this case.

4. IMPLIED TERMS: CUSTOM OR TRADE USAGE¹⁰²

13.16 A term can be implied to reflect the custom of a locality or the usage of a particular trade¹⁰³ and, as Parke B's decision in *Hutton v. Warren* (1836) shows,¹⁰⁴ this is possible even though the contract is in writing or it is a formal deed (5.03). This is because implied terms are an exception to the 'parol evidence rule'¹⁰⁵ (that rule operates in general to exclude evidence aimed at varying or supplementing written terms: see 14.26).

13.17 The relevant market usage must be 'universal and acknowledged' (as the House of Lords said in *Baker v. Black Sea & Baltic General Insurance Co. Ltd* (1998)).¹⁰⁶ Ungood-Thomas J, in the *Cunliffe-Owen* case (1967),¹⁰⁷ set out five criteria to govern recognition of an implied term based on custom:

- (1) The custom must be 'notorious'. In other words, the custom must be so readily ascertainable that the parties can be taken to have assented to it. For example, in *Turner v. Royal Bank of Scotland plc* (1999), a banking practice was held not to be notorious:¹⁰⁸ the relevant practice entailed banks divulging confidential information concerning their clients' accounts to third parties regarding creditworthiness.
- (2) The custom must be 'certain', that is, clearly established.

the relevant topic, see *ServicePower Asia Pacific Pty Ltd v. ServicePower Business Solutions Ltd* [2009] EWHC 179 (Ch); [2010] 1 All ER (Comm) 238, at [25] ff, William Trower QC (noted also at 16.30).

⁹⁸ [2009] EWCA Civ 531; [2009] 2 Lloyd's Rep 639.

⁹⁹ *Ibid.*, at [18].

¹⁰⁰ [1977] AC 239, HL.

¹⁰¹ [1995] EMLR 472, CA; Sir Bernard Rix, 'Lord Bingham's Contributions to Commercial Law', in M. Andenas and D. Fairgrieve (eds.), *Tom Bingham and the Transformation of the Law: A Liber Amicorum* (Oxford, 2009), 675.

¹⁰² R. Goode, 'Usage and its Reception in Transnational Commercial Law' (1997) 46 ICLQ 1–36.

¹⁰³ *Liverpool City Council v. Irwin* [1977] AC 239, 253, HL, *per* Lord Wilberforce; *Baker v. Black Sea & Baltic General Insurance Co. Ltd* [1998] 1 WLR 974, 983–4, HL, 979–80, 982–4, HL; *Turner v. Royal Bank of Scotland plc* [1999] 2 All ER (Comm) 664, CA.

¹⁰⁴ (1836) 1 M & W 466; 150 ER 517.

¹⁰⁵ M & W report, *ibid.*, at 475.

¹⁰⁶ [1998] 1 WLR 974, 983–4, HL, *per* Lord Lloyd.

¹⁰⁷ *Cunliffe-Owen v. Teather & Greenwood* [1967] 1 WLR 1421, 1438–9, Ungood-Thomas J (concerning customs of the London Stock Exchange).

¹⁰⁸ [1999] 2 All ER (Comm) 664, CA.

- (3) The custom must be 'reasonable'.¹⁰⁹
- (4) The custom must be not inconsistent with the contract's written terms: as the maxim states, *expressum facit cessare tacitum* ('what is spelt out overrides what is implicit').¹¹⁰ This point was acknowledged by the House of Lords in the *Leopold Walford* case (1919).¹¹¹
- (5) The custom must be perceived as binding in law. As the Court of Appeal held in the *General Reinsurance Corporation* case (1983), mere regularity of conduct is not enough, because it might be an expression of courtesy or concession.¹¹²

13.18 Establishing a custom is a mixed question of fact and law.¹¹³ Resort will often be had to experts to establish the requisite 'continuity of acts'.¹¹⁴ A pattern of conduct can be difficult to prove if (as can often occur) expert opinion is sharply divided.¹¹⁵ Questions might also arise not on whether a custom exists but on its precise ambit.¹¹⁶ Finally, the concept of 'trade usage' can be employed to justify incorporation of terms into a transaction between businessmen. On this basis, the Court of Appeal in *British Crane Hire Corporation Ltd v. Ipswich Plant Hire Ltd* (1975)¹¹⁷ held that the claimant's standard written term, which was widespread in the industry, had been impliedly incorporated into an urgently concluded oral contract of hire (provided the relevant term is 'reasonable'):¹¹⁸ '[B]oth parties knew quite well that conditions were habitually imposed by the supplier of these machines: and both parties knew the substance of those conditions.'¹¹⁹

5. IMPLIED TERMS AND THE TORT OF NEGLIGENCE

13.19 In many situations governed by contract, the tort of negligence will also impose liability for personal injury, physical damage or even economic loss (5.17) arising from careless performance of a duty assumed by the defendant. This tort and contractual implied terms often provide the same or a very similar regime of rights and duties in many standard relationships. For example, the Court of Appeal's decision in *Johnstone v. Bloomsbury Health Authority* (1992)¹²⁰ (13.07) concerned the position of junior doctors required to

109 *Robinson v. Mollett* (1875) LR 7 HL 802, 836–8, HL.

110 *Johnstone v. Bloomsbury Health Authority* [1992] 1 QB 333, CA (13.07, 13.20), noted by A. Weir, [1991] CLJ 397; adopted in *McLory v. Post Office* [1993] 1 All ER 457, 462D, David Neuberger QC, sitting as a Deputy High Court Judge.

111 *Les Affréteurs Réunis SA v. Leopold Walford (London) Ltd* [1919] AC 801, HL (cf *ibid.*, 808, for Lord Birkenhead's doubt concerning this custom).

112 *General Reinsurance Corporation v. Forsakringsaktiebolaget Fennia Patria* [1983] QB 856, 874, CA, per Slade LJ (custom in insurance market merely matter of 'grace' and so non-binding).

113 *Cunliffe-Owen v. Teather & Greenwood* [1967] 1 WLR 1421, 1438B, Ungood-Thomas J.

114 *Ibid.*, at 1438D–E.

115 E.g. *Libyan Arab Foreign Bank v. Bankers Trust Co.* [1989] QB 728, 755–60, per Staughton J (foreign bond market); R. Goode, (1997) 46 ICLQ 1, 8–9.

116 *Cunliffe-Owen* case, [1967] 1 WLR 1421, 1456E.

117 [1975] QB 303, CA.

118 *Ibid.*, at 314.

119 *Ibid.*, at 311B.

120 [1992] 1 QB 333, 340G, CA; noted by A. Weir, [1991] CLJ 397.

work very long hours within the National Health Service when qualifying to practise. Leggatt LJ and Browne-Wilkinson V-C noted the following principle contained in the *Tai Hing* case (1979) (13.20): '[The parties' mutual obligations in tort] cannot be any greater than those to be found expressly or by necessary implication in their contract.'¹²¹

- 13.20 But, at any rate in commercial disputes concerning economic loss, the courts are wary of permitting the law of negligence to outflank the settled regime of responsibility prescribed by implied terms. The courts do not permit tortious liability to operate inconsistently with the relevant contractual matrix of implied terms, as the Privy Council's decision in *Tai Hing Ltd v. Liu Chong Hing Bank* (1979) shows.¹²² The law of contract requires a bank's customer (1) to exercise care in drawing cheques so as not to facilitate fraud or forgery, and (2) to inform the bank at once of any unauthorised cheques of which he becomes aware. These two propositions were long ago fixed as implied terms.¹²³ Against this background, Lord Scarman protested in the *Tai Hing* case that it would be undesirable for the tort of negligence to muddy these clear contractual waters by imposing a wider duty of care upon a customer.¹²⁴
- 13.21 Similarly, Lord Bridge in the *Scally* case (1992)¹²⁵ (13.07) said that it would be 'positively misleading' to use the tort of negligence to determine whether an employer owed a responsibility to point out to an employee the financial benefit in taking advantage of a recently agreed collective agreement relating to pension entitlement. Instead, this issue fell under the rubric of contractual 'implied terms'.

6. IMPLIED TERMS AND GOOD FAITH

- 13.22 The general question concerning the merits of recognising a duty to perform contracts in good faith is examined at 21.03. As explained in detail there, English law has not adopted such a general doctrine. It is submitted that the selective and fact-sensitive technique of implying terms enables the English courts to do justice in a free and generous fashion. As we have seen in this chapter, this technique is also precise (prescribing rules for specific types of transactions, or even recognising 'one-off' terms implied *in fact*). It is a fair reading of the law concerning implied terms to conclude that there is no need (or, at least, very little practical need) to adopt the general criterion of commercial 'good faith'.
- 13.23 However, some judges have perhaps gone too far in proclaiming the capacity of contracting parties to act without regard to notions of fair dealing. These remarks no longer chime with modern approaches. In particular, Lord Reid in *White & Carter v. McGregor* (1962)

¹²¹ *Ibid.*, at 347E, 350A, CA.

¹²² [1979] AC 91, PC.

¹²³ *Ibid.*, at 108.

¹²⁴ *Ibid.*, at 107.

¹²⁵ *Scally v. Southern Health Board* [1992] 1 AC 294, 303–4, HL.

(on appeal from Scotland) said that in English law a contractual right or power need not be exercised reasonably, 'equitably' or in good faith:¹²⁶

It might be, but it never has been, the law that a person is only entitled to enforce his contractual rights in a reasonable way, and that a court will not support an attempt to enforce them in an unreasonable way. One reason why that is not the law is, no doubt, because it would create too much uncertainty to require the court to decide whether it is reasonable or equitable to allow a party to enforce his full rights under a contract.

Lord Reid's statement needs to be qualified, for he suggests that there is no attempt at all by the courts to control the exercise of contractual powers. The first reason for qualifying his statement is that recent authorities, including *Paragon Finance plc v. Nash* (2002),¹²⁷ cited at 13.13 above, adopt an (admittedly) restrictive approach to judicial regulation of a party's exercise of contractual discretion. A second noteworthy development is that the House of Lords in *Malik (and Mahmud) v. Bank of Credit and Commerce International SA* (1998) (13.07) recognised a general implied term that the employer should not behave in a way which will destroy or threaten the relationship of confidence and trust between him and his employees.¹²⁸ But that special relationship has been distinguished from other contexts. In *Jani-King (GB) Ltd v. Pula Enterprises Ltd* (2007), Coulson J noted that, in accordance with a settled line of cases, in ordinary commercial contracts there is no implied term that the parties will refrain 'from acting in such a way as to destroy or seriously damage the relationship of trust and confidence between them'.¹²⁹

- 13.24 Even if 'good faith' were introduced ('implied' or 'imposed') as a general requirement of contractual performance, this might be restricted to the *avoidance of dishonest conduct*. In that narrow sense, the courts might be willing to imply a term requiring honest conduct (just as the common law invalidates an attempt by an exclusion clause to exclude or restrict liability for fraud).¹³⁰ There is some support for the implied term that a party will refrain from dishonest conduct. In *Philips Electronique Grand Publique SA v. British Sky Broadcasting Ltd* (1995), Sir Thomas Bingham MR hinted that he would be prepared to find an implied term of that restricted nature (the case is considered

126 [1962] AC 413, 430, HL, *per* Lord Reid; similarly *Chapman v. Honig* [1963] 2 QB 502, 520–1, CA; cf *McLory v. Post Office* [1993] 1 All ER 457, 462–5, *per* David Neuberger QC, sitting as a Deputy High Court Judge; A. Weir, in P. Cane and J. Stapleton (eds.), *The Law of Obligations: Essays in Celebration of John Fleming* (Oxford, 1998), 123–4, citing *Balfour Beatty v. Docklands Light Railway* (1996) 78 BLR 49, CA.

127 *Paragon Finance plc v. Nash* [2001] EWCA Civ 1466; [2002] 1 WLR 685.

128 [1998] 1 AC 20, 45–6, HL, *per* Lord Steyn (recognition of new cause of action for 'stigma damages': loss to former employees of fraudulent employer when those former employees find it impossible to re-enter the same job market because of their association with their fraudulent former employer).

129 [2007] EWHC 2433 (QBD); [2008] 1 Lloyd's Rep 305, at [48] ff.

130 *S Pearson & Son Ltd v. Dublin Corporation* [1907] AC 351, 353, 362, HL; *HIH Casualty and General Insurance Ltd v. Chase Manhattan Bank* [2003] 2 Lloyd's Rep 61, HL, at [16], *per* Lord Bingham, and at [98] *per* Lord Hobhouse (see 15.04).

more fully at 13.14 above),¹³¹ although on the facts there had been no breach of ‘good faith’ in this sense.

- 13.25 More recently, a first instance *dictum* has suggested a bolder approach. Morgan J in *Berkeley Community Villages Ltd v. Pullen* (2007) suggested that an owner of land who had entered into a detailed written contract for the development of the land was obliged not to frustrate this venture by unilaterally selling the property to a third party:

[T]here are no sufficient countervailing arguments to overwhelm what I have described as the powerful arguments in favour of an implied term that the Defendants should not be free to sell the land during the term of the Agreement.¹³²

But this was a *dictum*: the main decision was that the defendant had breached a reciprocal *express term* imposing a duty of ‘utmost good faith’ and that this phrase was not uncertain. The better view is that Morgan J’s *obiter* comment – such a duty would be otherwise implicit – is merely a straw in the wind.

7. IMPLIED TERMS AND THE DOCTRINES OF MISTAKE AND FRUSTRATION

- 13.26 The interplay between these doctrines and the concept of an ‘implied term’ has a long judicial and scholarly history. As for the doctrine of frustration (on which see chapter 16), Blackburn J in the first modern decision, *Taylor v. Caldwell* (1863),¹³³ based the doctrine’s operation upon an implied term. But this theory was decisively rejected by Lord Radcliffe in *Davis Contractors Ltd v. Fareham Urban District Council* (1956)¹³⁴ and by Lord Denning MR in *The Eugenia* (1964)¹³⁵ as stretching reality and introducing a fictitious ‘tacit consent’ (these passages are quoted at 16.03). As for ‘mistake’, the implied term approach to cases of *initial impossibility* and other pre-formation errors took longer to dislodge. However, Lord Phillips in ‘*The Great Peace*’ emphatically rejected the implied theory of mistake (as noted at 10.07). He said that ‘the theory of the implied term is as unrealistic when considering common mistake as when considering frustration’, and added: ‘Avoidance of a contract on the ground of common mistake results from a rule of law.’¹³⁶ But, as *Graves v. Graves* (2007) (10.11) makes clear, the ghost of implied terms has not been exorcised from the sector of contract covered by mistake.¹³⁷

131 [1995] EMLR 472, CA.

132 [2007] EWHC 1330, Morgan J, at [141].

133 (1863) 3 B & S 826; 122 ER 309.

134 [1956] AC 696, HL.

135 *Ocean Tramp Tankers Corporation v. V/O Sovfracht* (‘*The Eugenia*’) [1964] 2 QB 226, 238, CA.

136 *Great Peace Shipping Ltd v. Tsavliris Salvage (International) Ltd* [2003] QB 679, CA, at [73].

137 [2007] EWCA Civ 660; [2008] HLR 10; [2008] L & TR 15; [2007] 3 FCR 26.

Chapter contents

1. Introduction *para.* 14.01
2. Written contracts and questions of 'law' *para.* 14.03
3. Main rules governing the interpretation of written contracts *para.* 14.06
4. The pre-contractual negotiation bar *para.* 14.13
5. 'Interpretation' to eliminate obvious or demonstrable errors *para.* 14.21
6. Interpretation and the parol evidence rule *para.* 14.26
7. Interpretation and implied terms *para.* 14.32
8. Rectification *para.* 14.33

14

Interpretation and rectification of written contracts

1. INTRODUCTION¹

14.01 Summary of main points

- (1) 'Interpretation [of written contracts] is the ascertainment of meaning which the document would convey to a reasonable person having all the background knowledge which would reasonably have been available to the parties in the situation in which they were at the time of the contract.' See the quotation from Lord Hoffmann in the *Investors Compensation Scheme* case (1998) at 14.07.
- (2) Interpretation of written contracts is a matter of law, whereas interpretation of contracts not wholly contained in writing is a matter of fact (14.03). Appeal courts have the power to review first instance errors of 'law', but in general defer to findings of fact.

¹ Main textbooks: K. Lewison, *Interpretation of Contracts* (4th edn, London, 2007); G. McMeel, *The Construction of Contracts: Interpretation, Implication and Rectification* (Oxford, 2007) (see also McMeel's articles in [1998] LMCLQ 382, (2003) 119 LQR 272, (2005) 34 *Common Law World Review* 256 and [2006] LMCLQ 49; and McMeel, 'The Principles and Policies of Contractual Construction', in A. Burrows and E. Peel (eds.), *Contract Terms* (Oxford, 2007), chapter 3); Catherine Mitchell, *Interpretation of Contracts* (London, 2007). Other discussion: Lord Bingham, 'A New Thing Under the Sun: The Interpretation of Contract and the ICS Decision' (2008) 12 *Edinburgh Law Review* 374; R. Buxton, '"Construction" and Rectification After Chartbrook' [2010] CLJ 253; J. Cartwright, 'Interpretation of English Law in Light of the Common Frame of Reference', in H. Snijders and S. Vogenauer (eds.), *Content and Meaning of National Law in the Context of Transnational Law* (Munich, 2009); Lord Hoffmann, 'The Intolerable Wrestle with Words and Meanings' (1997) *South Africa Law Journal* 656; E. McKendrick, in S. Worthington (ed.), *Commercial Law and Commercial Practice* (Oxford, 2003); D. McLauchlan, 'Contract Interpretation: What Is It About?' (2009) 31 *Sydney Law Review* 5; Lord Nicholls, 'My Kingdom for a Horse: The Meaning of Words' (2005) 121 LQR 577; Lord Phillips, 'The Interpretation of Contracts and Statutes' (2002) 68 *Arbitration* 17; Spigelmann CJ, 'From Text to Contract: Contemporary Contractual Interpretation' (2007) 81 ALJ 322; Sir Christopher Staughton, 'How Do the Courts Interpret Commercial Contracts?' [1999] CLJ 303; Lord Steyn, 'Written Contracts: To What Extent May Evidence Control Language?' (1988) 41 CLP 23; C. Valcke, 'On Comparing French and English Contract Law: Insights from Social Contract Theory' (2009): <http://lsolum.typepad.com/legaltheory/2009/01/valcke-on-compa.html>; S. Vogenauer, 'Interpretation of Contracts: Concluding Comparative Observations', in A. Burrows and E. Peel (eds.), *Contract Terms* (Oxford, 2007), chapter 7.

- (3) The House of Lords in *Chartbrook Ltd v. Persimmon Homes Ltd* (2009) held that a court can 'construe' by wholly recasting a relevant phrase or portion of a written contract when it is obvious that the drafting has gone awry and the parties' true pre-formation shared meaning can be ascertained by consideration of the commercial purpose of the agreement and internal hints in the text (14.21 ff). Such 'curative interpretation' has a similar function to the more formal equitable doctrine of 'rectification' (see (9) below), because both doctrines have the effect of revising a document. The safer course is to plead both 'construction' and 'rectification'.
- (4) Lord Mustill in *Charter Reinsurance Co. Ltd v. Fagan* (1997) (14.09) said that it is illegitimate for courts or arbitrators to 'force upon the words a meaning which they cannot fairly bear', since this would be 'to substitute for the bargain actually made one which the court believes could better have been made'.
- (5) The courts are not tied to the literal wording of the written contract, but can consider the parties' common intention against the background of the transaction. However, in making this extended search, Lord Hoffmann in the *BCCI* case (2001)² (14.11) said that courts and arbitrators should control attempts by parties to adduce excessive quantities of background information.
- (6) In the *Sigma* case (2009) (14.12), Lord Collins (with the support of Lords Mance and Hope) disapproved³ too broad a search for background information (see in general (5) above) when, as in the *Sigma* case itself, the parties to the relevant transaction might not have been present at its birth, and had instead become second-hand or remoter recipients of others' contractual text which had been in circulation in the relevant financial market.
- (7) When seeking to interpret written contracts, a party cannot adduce, without his opponent's permission, the parties' prior negotiations. The fivefold rationale for this bar is considered to be (14.15): (i) avoidance of 'uncertainty and unpredictability'; (ii) the fact that interested third parties cannot be guaranteed access to such negotiation history; (iii) such dealings are notoriously shifting and so such evidence would be unhelpful; (iv) one-sided impressions might contaminate the inquiry so that the objective approach to interpretation (see (1) above) would be undermined; and (v) 'sophisticated and knowledgeable negotiators would be tempted to lay a paper trail of self-serving documents'.

² [2001] 1 AC 251, at [39], HL.

³ *In Re Sigma Finance Corporation (in administrative receivership)* [2009] UKSC 2; [2010] 1 All ER 571; [2010] BCC 40, at [35] to [37].

- (8) But this evidential bar does not apply to the equitable remedy of rectification (on which see (9) and (10) below, and 14.33 ff). And so claims for rectification are often brought in conjunction with a pleading based on ordinary 'interpretation' (as in the *Chartbrook* case itself).⁴
- (9) Rectification is an equitable remedy allowing the court to declare that a written contract should be reconstituted to reflect the parties' 'common continuing intention' provided this has been 'outwardly' expressed: the doctrine requires:
 - (i) ... a common continuing intention, whether or not amounting to an agreement, in respect of a particular matter in the instrument to be rectified; (ii) that there was an outward expression of accord; (iii) that the intention continued at the time of the execution of the instrument sought to be rectified; and (iv) that by mistake the instrument did not reflect that common intention.⁵
- (10) A mere unilateral error does not support a claim for rectification, unless the other party's position is wholly unmeritorious, in particular, because he has dishonestly acquiesced in the other's mistake (14.42 ff).

Interpretation is the 'hottest' topic in English contract law. It has produced a massive recent literature. These are some of the leading discussions of the interrelated topics appearing in this chapter:

Investors Compensation Scheme (1998) Principles of Interpretation for Written Contracts

- E. McKendrick, 'The Interpretation of Contracts: Lord Hoffmann's Restatement', in S. Worthington (ed.), *Commercial Law and Commercial Practice* (Oxford, 2003)
- Lord Nicholls, 'My Kingdom for a Horse: The Meaning of Words' (2005) 121 LQR 577, especially 585–8 (although Lord Hoffmann in *Chartbrook* did not find persuasive Lord Nicholls' plea in that article for abolition of the rule barring evidence of negotiations as an aid to interpretation of written contracts)
- A. Berg, 'Thrashing Through the Undergrowth' (2006) 122 LQR 354, especially 358–62
- R. Buxton, '"Construction" and Rectification After Chartbrook' [2010] CLJ 253

⁴ [2009] UKHL 38; [2009] 1 AC 1101.

⁵ *Swainland Builders Ltd v. Freehold Properties Ltd* [2009] UKHL 38; [2009] 1 AC 1101, per Peter Gibson LJ, cited at 14.34.

The approach of other legal systems to pre-contractual negotiations as aid to interpretation

- E. Clive, in H. MacQueen and R. Zimmermann (eds.), *European Contract Law: Scots and South African Perspectives* (Edinburgh, 2006), chapter 7, at 183
- M. J. Bonell (ed.), *The UNIDROIT Principles in Practice: Case Law and Bibliography on the UNIDROIT Principles of International Commercial Contracts* (2nd edn, Ardsley, NY, 2006), 234 ff
- S. Vogenauer and J. Kleinheisterkamp (eds.), *Commentary on the UNIDROIT Principles of International Commercial Contracts* (Oxford, 2009), 510 ff

Equitable doctrine of rectification

- M. Smith, 'Rectification of Contracts for Common Mistake' (2007) 123 LQR 116, especially 130 ff
- D. McLauchlan, 'The "Drastic" Remedy of Rectification for Unilateral Mistake' (2008) 124 LQR 608–40, especially 608–10 and 639–40

Relationship between interpretation to iron out drafting snags and rectification in equity

- A. Burrows, 'Construction and Rectification', in A. Burrows and E. Peel (eds.), *Contract Terms* (Oxford, 2007) 77, especially 90 ff

Comparative discussion

- C. Valcke, 'Contractual Interpretation at Common Law and Civil Law: An Exercise in Comparative Legal Rhetoric', in J. W. Neyers, R. Bronaugh and S. G. A. Pitel (eds.), *Exploring Contract Law* (Oxford, 2009), 77 ff

14.02 For contract draftsmen and all those concerned with contractual disputes, this is probably the most important topic within contract law.⁶ The subject overlaps with other doctrines: the objective principle of contractual dealings; the equitable doctrine of rectification (see 14.33 ff); the common law attitude to exclusion of other 'onerous' clauses (15.02); and the implication of terms as a matter of *fact* or *law* (see chapter 13). McMeel's wide-ranging book (2007) reflects this complex interaction between various doctrines.⁷ The subject has become controversial. English law retains a deliberately 'blinker' approach to interpretation, in the sense that the court is in general denied access either to the parties' prior negotiations (the biggest controversy: see 14.13 ff) or to the parties' subsequent conduct. This contrasts, as we shall see, with the approach adopted in many other legal systems and in the influential 'soft law'

6 E.g. Sir Christopher Staughton, [1999] CLJ 303; A. Burrows, 'Construction and Rectification', in A. Burrows and E. Peel (eds.), *Contract Terms* (Oxford, 2007), 77–8.

7 G. McMeel, *The Construction of Contracts: Interpretation, Implication and Rectification* (Oxford, 2007), chapter 1 (overview of the topic), chapters 10 to 12 (implied terms), chapter 17 (rectification), chapter 18 (estoppel by convention), chapter 20 (categorisation of primary terms as 'conditions', 'innominate terms' and 'warranties') and chapter 21 (exemption clauses).

codes (14.16). The House of Lords in *Chartbrook Ltd v. Persimmon Homes Ltd* (2009)⁸ held that there is no justification for judicial reversal of the exclusionary rule concerning prior negotiations (14.14).

2. WRITTEN CONTRACTS AND QUESTIONS OF 'LAW'

- 14.03 Contracts can be formed by conduct or by words, or by a combination of the two. Interpretation of (wholly) 'written contracts' (including electronic documents)⁹ is a question of law,¹⁰ and this means that (if permission to appeal is obtained) an appellate court will have the opportunity to reconsider the lower court's view of the contract's effect¹¹ (or the point *might* be subject to appeal from an arbitration tribunal, if the High Court gives permission).¹² By contrast, appellate courts are generally reluctant to re-open findings of fact made by first instance courts (although the precise scope of appeals against matters of fact has become a complex field of procedure).

The appellate court's capacity to re-open findings of fact depends on the manner in which the first instance court has reached the relevant finding:¹³

In appeals against conclusions of primary fact the approach of an appellate court will depend upon the weight to be attached to the findings of the judge and that weight will depend upon the extent to which, as the trial judge, the judge has an advantage over the appellate court; the greater that advantage the more reluctant the appellate court should be to interfere.¹⁴

The 'advantage' is the lower court's monopoly (under modern practice) upon hearing live testimony.

However, not all civil cases involving interpretation need to go to trial. Some points of construction are amenable to summary judgment, without waiting for witness evidence to be garnered and presented at trial. In *ICI Chemicals & Polymers Ltd v. TTE Training Ltd* (2007), Moore-Bick LJ said: '[I]f the court is satisfied that it has before it all the evidence necessary for the proper determination of the question and that the parties have had an adequate opportunity to address it in argument, it should grasp the nettle and decide it.'¹⁵ However, final disposal by summary judgment is unavailable if

8 [2009] UKHL 38; [2009] 1 AC 1101 (noted by D. McLaughlan, (2010) 126 LQR 8–14).

9 *Chitty on Contracts* (30th edn, London, 2008), 12–048; G. McMeel, *The Construction of Contracts: Interpretation, Implication and Rectification* (Oxford, 2007), 26–01 to 26–17.

10 *Chitty on Contracts* (30th edn, London, 2008), 12–046.

11 E.g. *AXA Reinsurance (UK) v. Field* [1996] 1 WLR 1026, HL.

12 N. Andrews, *Contracts and English Dispute Resolution* (Tokyo, 2010), 21.05, noting section 69 of the Arbitration Act 1996 (England); scope for granting leave to appeal from an arbitrator's decision is constrained: *ibid.*, section 69(3); *Russell on Arbitration* (22nd edn, London, 2003), 8–054 ff.

13 *Datec Electronics Holdings Ltd v. United Parcels Services Ltd* [2007] UKHL 23; [2007] 1 WLR 1325, at [46], Lord Mance, quoting Clarke LJ in *Assicurazioni Generali SpA v. Arab Insurance Group* [2002] EWCA Civ 1642; [2003] 1 WLR 577, CA.

14 *Assicurazioni Generali SpA v. Arab Insurance Group* [2002] EWCA Civ 1642; [2003] 1 WLR 577, CA, at [15], *per* Clarke LJ.

15 [2007] EWCA Civ 725, at [12]; *Royal Bank of Scotland plc v. Highland Financial Partners LP* [2010] EWCA Civ 809.

the point of interpretation requires reference to facts which are not agreed; for example, references to market practice require the receipt of expert evidence.¹⁶

- 14.04 The High Court, and higher courts, can decide disputes on interpretation of written contracts which will provide a valuable stream of precedent decisions on standard commercial words or phrases. As Lord Diplock said in the *Pioneer Shipping* case (1981):

It is only if parties to commercial contracts can rely on a uniform construction being given to standard terms that they can prudently incorporate them in their contracts without the need for detailed negotiation or discussion.¹⁷

He added:

Such uniform construction of standard terms had been progressively established up to 1979, largely through decisions of the courts on special cases stated by arbitrators. In the result English commercial law has achieved a degree of comprehensiveness and certainty that has made it acceptable for adoption as the appropriate proper law to be applied to commercial contracts wherever made by parties of whatever nationality.

Similarly, Lord Hoffmann said in the *Carmichael* case (1999):

[Classification of interpretation issues in written contracts as matters of law] was adopted in trials by jury for purely pragmatic reasons. In mediaeval times juries were illiterate and most of the documents which came before a jury were deeds drafted by lawyers ... There could have been no precedent and no certainty in the construction of standard commercial documents if questions of construction had been left in each case to a jury which gave no reasons for its decision.¹⁸

- 14.05 The question whether, on an objective view, the parties intended a written agreement to be an exclusive statement of their contract is a matter of fact to be ascertained from all the evidence. But there is a presumption (see the discussion of the parol evidence rule at 14.26 ff) that a written contract does in fact embrace all relevant terms. In the *Carmichael* case (1999),¹⁹ the House of Lords decided that the terms of the legal relationship were to be found in a mix of written and oral exchanges between the parties. The following statements attempt to provide a test for this purpose:²⁰

[I]t would only be appropriate to determine the issue in these cases solely by reference to the documents ... if it appeared from their own terms and/or from what the parties

16 *International Private Equity Ltd v. ABN Amro Bank NV* [2009] EWHC 2523 (Ch), at [15], per Warren J.

17 *Pioneer Shipping Ltd v. BTP Tioxide Ltd ('The Nema')* [1982] AC 724, 737, HL.

18 *Carmichael v. National Power plc* [1999] UKHL 47; [1999] 1 WLR 2042.

19 *Ibid.*, at 2049.

20 *Ibid.*, at 2047C, 2049, per Lord Irvine LC.

said or did then, or subsequently, that they intended them to constitute an exclusive memorial of their relationship.

And:

[The exclusionary rules] about the construction of documents ... [apply] in cases in which the parties intend all the terms of their contract (apart from any implied by law) to be contained in a document or documents. [But they do not] apply when the intention of the parties, objectively ascertained, has to be gathered partly from documents but also from oral exchanges and conduct. In the latter case, the terms of the contract are a question of fact. And of course the question of whether the parties intended a document or documents to be the exclusive record of the terms of their agreement is also a question of fact.²¹

In *Thorner v. Major* (2009) (2.05; and see case (3) at 5.66), Lord Neuberger explained:²²

[Although] (a) the interpretation of a purely written contract is a matter of law, and depends on a relatively objective contextual assessment, which almost always excludes evidence of the parties' subjective understanding of what they were agreeing ... (b) the interpretation of an oral contract is a matter of fact (I suggest inference from primary fact), rather than one of law, on which the parties' subjective understanding of what they were agreeing is admissible.

The reason for this dichotomy is partly historical. Juries were often illiterate, and could therefore not interpret written contracts, whereas they could interpret oral ones. But it also has a good practical basis. If the contract is solely in writing, the parties rarely give evidence as to the terms of the contract, so it is cost-effective and practical to exclude evidence of their understanding as to its effect. On the other hand, if the contract was made orally, the parties will inevitably be giving evidence as to what was said and done at the relevant discussions or meetings, and it could be rather artificial to exclude evidence as to their contemporary understanding. Secondly, and perhaps more importantly, memory is often unreliable and self-serving, so it is better to exclude evidence of actual understanding when there is no doubt as to the terms of the contract, as when it is in writing. However, it is very often positively helpful to have such evidence to assist in the interpretation of an oral contract, as the parties will rarely, if ever, be able to recollect all the details and circumstances of the relevant conversations.

3. MAIN RULES GOVERNING THE INTERPRETATION OF WRITTEN CONTRACTS

14.06 There are six main propositions:

²¹ *Ibid.*, per Lord Hoffmann.

²² [2009] UKHL 18; [2009] 1 WLR 776, at [82] and [83].

Leading proposition 1

The ‘objective principle of agreement’ precludes reference to a party’s undisclosed and personal understanding of the written terms’ meaning and effect.²³

Leading proposition 2

Evidence of pre-formation negotiations is not normally admissible (14.14 ff).

For three exceptions, see 14.20. In particular, evidence of negotiations is admissible for the purpose of rectification, an independent equitable remedy (14.33 ff). Furthermore, background evidence is admitted to determine the ‘genesis’ or ‘aim’ of the contract (see ‘Leading proposition 5’ below).

The Supreme Court in *Oceanbulk Shipping and Trading SA v. TMT Asia Ltd* (2010)²⁴ held that ‘without prejudice’ negotiations, which resulted in a settlement agreement, can be admitted for the purpose of ascertaining the factual matrix of the relevant agreement. In light of that background material, the court could then interpret the terms of the settlement. To decide otherwise would be to create an unprincipled distinction between interpretation of all other commercial contracts and interpretation of settlement agreements. Lord Clarke, giving the court’s judgment, said:²⁵

I see no reason why the ordinary principles governing the interpretation of a settlement agreement should be any different regardless of whether the negotiations which led to it were without prejudice. The ... question ... should be the same, namely what a reasonable person having all the background knowledge which would have been available to the parties would have understood them to be using the language in the contract to mean. That background knowledge may well include objective facts communicated by one party to the other in the course of the negotiations. As I see it, the process of interpretation should in principle be the same, whether the negotiations were without prejudice or not. In both cases the evidence is admitted in order to enable the court to make an objective assessment of the parties’ intentions.

Leading proposition 3

A written contract should not be construed by reference to the parties’ conduct subsequent to the contract’s formation.²⁶

23 *Reardon Smith Line Ltd v. Hansen Tangen* [1976] 1 WLR 989, 996, HL, *per* Lord Wilberforce.

24 [2010] UKSC 44; [2010] 3 WLR 1424, reversing the Court of Appeal, [2010] EWCA Civ 79; [2010] 1 WLR 1803 (Longmore and Stanley Burnton LJ; Ward LJ dissenting).

25 *Ibid.*, at [40].

26 *L Schuler AG v. Wickman Machine Tool Sales* [1974] AC 235, 252, 260, 261, 266–9, 272–3, HL, affirming the rule in *Whitworth Street Estates (Manchester) Ltd v. James Miller & Partners Ltd* [1970] AC 583, HL; A. Berg, (2008) 124 LQR 6–15, noting Thomas J’s attack on this bar in *Wholesale Distributors Ltd v. Gibbons Holdings Ltd* [2007] NZSC 37; [2008] 1 NZLR 277 (Elias CJ, Tipping and Anderson JJ agreeing; Blanchard J reserving his position).

Thus, subsequent conduct cannot retroactively shed light on the original shared understanding. Lord Reid said in *Whitworth Street Estates (Manchester) Ltd v. James Miller & Partners Ltd* (1970) that the reason for the rule is that ‘otherwise one might have the result that a contract meant one thing the day it was signed, but by reason of subsequent events meant something different a month or a year later.’²⁷ However, Burrows has challenged this rationale. He suggests that ‘this is a *non sequitur* given that one is trying to ascertain only what the contract meant at the time it was made. One is not rewriting the contract with hindsight.’²⁸

It should be noted that this rule applies only to *wholly written* contracts and not to oral agreements, nor to contracts which are part oral and part written. In *Maggs v. Marsh* (2006), Smith LJ said:²⁹

Determining the terms of an oral contract is a question of fact. Establishing the facts will usually, as here, depend upon the recollections of the parties and other witnesses. The accuracy of those recollections may be tested and elucidated by things said and done by the parties or witnesses after the agreement has been concluded. Receiving evidence of such words or actions does not mean that the judge is losing sight of his task of deciding what the parties agreed at the time of the contract. It is simply helping him to decide whose recollection is right.

As for purely oral agreements, in *Carmichael v. National Power plc* (1999), Lord Hoffmann said that the court can receive ‘evidence of subsequent conduct [which] shows what the parties thought they had agreed ... [or] to support an argument that the terms have been varied or enlarged or to found an estoppel’.³⁰

Furthermore, even in the case of contracts *wholly contained in writing*, exceptions to the present bar exist:

- (1) if it can be shown that the parties had specifically agreed to vary or discharge the agreement;³¹ or
- (2) if the doctrine of estoppel by convention (5.68, 14.20) can be established, that is, proof that, subsequent to formation, the parties had implicitly agreed on how the written terms should be interpreted or modified. To establish such an estoppel, an implicit agreement must be manifested in their pattern of behaviour and interaction. In *Amalgamated Investment & Property Co. Ltd v. Texas Commerce International Bank Ltd* (1982), Lord Denning MR explained:

So here we have ... evidence of subsequent conduct to come to our aid. It is available – not so as to construe the contract – but to see how they themselves acted on it. Under the guise of estoppel [by convention] we can

27 [1970] AC 583, 603, HL.

28 A. Burrows, ‘Construction and Rectification’, in A. Burrows and E. Peel (eds.), *Contract Terms* (Oxford, 2007), 77, 81 n. 21.

29 [2006] EWCA Civ 1058, at [25] and [36].

30 [1999] UKHL 47; [1999] 1 WLR 2042, 2051.

31 *Chitty on Contracts* (30th edn, London, 2008), 12-111.

prevent either party from going back on the interpretation they themselves gave to it.³²

Leading proposition 4

The courts should construe written instruments, including contracts, in a 'commercial' way, with sensitivity to business 'common sense'.

Lord Diplock said in *Antaios Cia Naviera SA v. Salen Rederierna AB* (1985):³³

[I]f detailed semantic and syntactical analysis of words in a commercial contract is going to lead to a conclusion that flouts business common sense, it must be made to yield to business common sense.

Lord Steyn said in *Mannai Investment Co. v. Eagle Star Life Assurance* (1997):³⁴

[A] commercial construction is more likely to give effect to the intention of the parties. Words are therefore interpreted in the way in which a reasonable commercial person would construe them. And the standard of the reasonable commercial person is hostile to technical interpretations and undue emphasis on niceties of language.

Leading proposition 5

To avoid the hazard of conducting interpretation 'in a vacuum', the courts permit the parties to refer to the contractual setting; and this perspective is expressed variously as consideration of the transaction's 'commercial purpose', 'genesis', 'background', 'context' and its location in the relevant 'market'.

On this see, in particular, Lord Wilberforce in the *Reardon Smith Line* case (1976).³⁵

Leading proposition 6

The courts will adopt a contextual approach to interpretation rather than a narrow 'dictionary meaning' approach ('semantic and syntactical').

This final proposition – emphasising the courts' willingness to adopt a non-literal, more liberal, approach – is the gist of Lord Hoffmann's long and seminal exposition of the

³² [1982] QB 84, 120, CA.

³³ [1985] AC 191, 201, HL.

³⁴ [1997] AC 749, HL (a majority decision concerning a rent notice); P. V. Baker, (1998) 114 LQR 55–62; see also his extra-judicial comments on this topic: J. Steyn, [1988] CLP 23, [1996] CLP 43, (1997) 113 LQR 433, (2003) 25 *Sydney Law Review* 5, and in B. Markesinis (ed.), *The Clifford Chance Millennium Lectures: The Coming Together of the Common Law and the Civil Law* (Oxford, 2000), Essay 5. On Lord Steyn's contribution to interpretation, see E. McKendrick, in S. Worthington (ed.), *Commercial Law and Commercial Practice* (Oxford, 2003), 158 n. 86.

³⁵ Lord Wilberforce in *Reardon Smith Line Ltd v. Hansen Tangen* [1976] 1 WLR 989, 995–6, HL; see Sir Christopher Staughton, [1999] CLJ 303, on the problem of the 'factual matrix'.

applicable principles in *Investors Compensation Scheme Ltd v. West Bromwich Building Society* (1998)³⁶ (although he attributed the real impulse for this approach to decisions in the 1970s).³⁷ We now turn to Lord Hoffmann's important formulations of principle in that decision.

14.07 *Lord Hoffmann's seminal statement in the Investors Compensation Scheme case (1998)*.³⁸

This case concerned a scheme for the compensation of victims of financial mismanagement. The upshot of the House of Lords decision was to rewrite a phrase so that, instead of an assignee receiving the benefit of rights of claim generally, the rights received were merely claims to rescind the relevant transactions (in his dissent, Lord Lloyd said that he found this form of creative interpretation simply unacceptable). The following passages in Lord Hoffmann's leading speech in *Investors Compensation Scheme* (1998) are already canonical (and were so treated by the Supreme Court in the *Sigma* case, 2009 (14.12)):³⁹

(i) Interpretation is the ascertainment of meaning which the document would convey to a reasonable person having all the background knowledge which would reasonably have been available to the parties in the situation in which they were at the time of the contract.

(ii) The background [has been described] as the 'matrix of fact', but this phrase is, if anything, an understated description of what the background may include, subject to the requirement that it should have been reasonably available to the parties and to the exception to be mentioned next, it includes absolutely anything which would have affected the way in which the language of the document would have been understood by a reasonable man.

(iii) The law excludes from the admissible background the previous negotiations of the parties and the declarations of subjective intent.⁴⁰ The law makes this distinction for reasons of practical policy and, in this respect only, legal interpretation differs from the way we would interpret utterances in ordinary life. The boundaries of this exception are unclear. But this is not the occasion on which to explore them.

(iv) The meaning which a document (or any other utterance) would convey to a reasonable man is not the same thing as the meaning of words. The meaning of words is a matter of dictionaries and grammars; the meaning of the document is what the

36 [1998] 1 WLR 896, 912–13, HL; E. McKendrick, in S. Worthington (ed.), *Commercial Law and Commercial Practice* (Oxford, 2003), 139–62.

37 *Prenn v. Simonds* [1971] 1 WLR 1381, 1384–6, HL; and *Reardon Smith Line Ltd v. Hansen Tangen* [1976] 1 WLR 989, HL; in the *Prenn* case, at 1384, Lord Wilberforce traced the 'anti-literal' approach to mid-nineteenth-century case law; on the *Reardon* case, see M. Bridge, in C. Mitchell and P. Mitchell (eds.), *Landmark Cases in the Law of Contract* (Oxford, 2008), 321 ff.

38 [1998] 1 WLR 896, 912–13, HL.

39 *In Re Sigma Finance Corporation (in administrative receivership)* [2009] UKSC 2; [2010] 1 All ER 571; [2010] BCC 40, at [10].

40 *Prenn v. Simonds* [1971] 1 WLR 1381, 1383G, HL.

parties using those words against the relevant background would reasonably have been understood to mean. The background may not merely enable the reasonable man to choose between the possible meanings of words which are ambiguous but even (as occasionally happens in ordinary life) to conclude that the parties must, for whatever reason, have used the wrong words or syntax.

(v) The ‘rule’ that words should be given their ‘natural and ordinary meaning’ reflects the common sense proposition that we do not easily accept that people have made linguistic mistakes, particularly in formal documents. On the other hand, if one would nevertheless conclude from the background that something must have gone wrong with the language, the law does not require judges to attribute to the parties an intention which they plainly could not have had.

Attention is also drawn to the succinct and careful distillation of principles (agreed by the parties) in Simon J’s judgment in *HHR Pascal BV v. W2005 Puppet II BV* (2009):⁴¹ (edited here by the combining of propositions to form a composite point (2) below):

(1) In interpreting the meaning of words in a contract the court must ascertain ... ‘the meaning which the document would convey to a reasonable person having all the background knowledge which would reasonably have been available to the parties in the situation in which they were at the time of the contract’. See Lord Hoffmann in the *ICS* case [1998] 1 WLR 896, 912.

(2) The principle that words should be given their natural and ordinary meaning reflects a common sense proposition that people do not usually make linguistic mistakes in formal documents. On the other hand, ‘if detailed semantic and syntactical analysis of words in a commercial contract is going to lead to a conclusion that flouts business commonsense, it must be made to yield to business commonsense’. See Lord Diplock in the *Antaios* case [1985] AC 191, 201, HL (quoted by Lord Hoffmann in the *ICS* case). Similarly, ‘In determining the meaning of the language of a commercial contract, and unilateral contractual notices, the law ... generally favours a commercially sensible construction. The reason for this approach is that a commercial construction is more likely to give effect to the intention of the parties. Words are therefore interpreted in the way in which a reasonable commercial person would construe them. And the standard of the reasonable commercial person is hostile to technical interpretations and undue emphasis on the niceties of language’. See Lord Steyn in the *Mannai* case [1997] AC 749, 771.

(3) A commercially sensible construction does not mean that the Court disregards express and clear terms in order to give effect to a conception of what might be fair or reasonable.

41 [2009] EWHC 2771 (Comm); [2010] 1 All ER (Comm) 399, at [35].

14.08 *Assessment of the Investors Compensation Scheme principles.* These principles permit the courts, where appropriate, to avoid a rigidly semantic or ‘dictionary-meaning’ style of interpretation provided the proposed non-literal interpretation is (1) supported by such background material as the court permits and (2) it is consistent with the objective perspective of the hypothetical ‘reasonable’ reader (who is not a flesh-and-blood party to the relevant contract: *Investors Compensation Scheme* principle (i), cited above at 14.07). As Benjamin Cardozo (the American judge) said in *Utica City National Bank v. Gunn* (1918), ‘it is easier to give a new shade of meaning to a word than to give no meaning to a whole transaction.’⁴²

14.09 But the courts must not illegitimately rewrite the contract.⁴³ In the *Rainy Sky* case (2010)⁴⁴ in the Court of Appeal, Patten LJ said:⁴⁵

Unless the most natural meaning of the words produces a result which is so extreme as to suggest that it was unintended, the Court has no alternative but to give effect to its terms. To do otherwise would be to risk imposing obligations on one or other party which they were never willing to assume and in circumstances which amount to no more than guesswork on the part on the Court.

In *Kookmin Bank v. Rainy Sky SA*, the dispute involved interpretation of bonds. Those bonds, issued by a third party, concerned repayment by a shipyard of prepayments for the purchase of ships under construction. A majority of the Court of Appeal (Tuckey LJ dissenting) held that the bonds’ wording did not expose the third party to make payment to cover the shipyard’s inability to repay following that shipyard’s insolvency.

But, in his dissent, and approving Simon J’s first instance decision, Tuckey LJ described the majority’s construction as wholly uncommercial:⁴⁶

[I]t makes no commercial sense. As [Simon J] said, insolvency of [the shipyard] was the situation for which the security of an advance payment bond was most likely to be needed. The importance attached in these contracts to the obligation to refund in the event of insolvency can be seen from the fact that they required the refund to be made immediately. It defies commercial common sense to think that this, among all other such obligations, was the only one which the parties intended should not be secured. Had the parties intended this surprising result I would have expected the contracts and the bonds to have spelt this out clearly but they do not do so.

The ‘knife-edge’ nature of this Court of Appeal majority decision is evident from the second member of the majority’s almost apologetic comments. Thorpe LJ said:⁴⁷

42 118 NE 607, 608 (NY Court of Appeals, 1918) (quoted in the *Reardon Smith* case, [1976] 1 WLR 989, 996, HL).

43 E. McKendrick, in S. Worthington (ed.), *Commercial Law and Commercial Practice* (Oxford, 2003), 139, 157 ff; see Lord Mustill in *Charter Reinsurance Co. Ltd v. Fagan* [1997] AC 313, 388, HL (quoted in the text in the present paragraph, below).

44 Permission to appeal has been granted by the Supreme Court, July 2010.

45 *Kookmin Bank v. Rainy Sky SA* [2010] EWCA Civ 582; [2010] 1 CLC 829, at [42].

46 *Ibid.*, at [30].

47 *Ibid.*, at [53].

I find myself in the invidious position of expressing a decisive opinion in a field that is completely foreign. With considerable trepidation I support the judgment of Patten LJ.

Similarly, Lord Mustill in *Charter Reinsurance Co. Ltd v. Fagan* (1997) spoke of the illegitimacy of ‘forcing upon the words a meaning which they cannot fairly bear’, since this would be ‘to substitute for the bargain actually made one which the court believes could better have been made’.⁴⁸

The House of Lords decision in that case (affirming Mance J and a majority of the Court of Appeal) is instructive because it demonstrates the pitfall of becoming attached to one’s ‘first blush’ and seemingly ‘common-sense’ reading of commercial words. The question was whether a reinsurer had agreed to indemnify the reinsured only if the latter’s liability had accrued, been quantified, and been discharged by payment (the so-called ‘actual disbursement’ interpretation) or whether it was enough that the liability to indemnify had arisen and been quantified, without actual discharge of that liability (the liability to pay or finalised quantification interpretation). The semantic battle was fought over the words ‘actually paid’.

The House of Lords agreed with the lower courts’ view that a commercially sensitive reading of that phrase in this particular reinsurance agreement led to this conclusion (admittedly surprising, because it appears to be the very opposite of one’s first understanding): the contract did not create a condition precedent to the reinsurer’s liability that the reinsured should actually have discharged the relevant liability.

- 14.10 Some judges, notably, Sir Christopher Staughton (a former Lord Justice of Appeal)⁴⁹ and Lightman J,⁵⁰ have suggested that permitting the parties to refer to background material (see ICS case principle (i) at 14.07) might induce parties to deluge the court with masses of material adduced to provide details of the document’s background or ‘factual matrix’. Lightman J has suggested that the parties should be required to offer a detailed pleading of that ‘matrix’.⁵¹ Berg suggests that ‘admissible background [material] should be limited to the sort of facts likely to be readily available to a lawyer asked to advise in circumstances in which a decision has to be taken without delay as to the course of action to be taken under the contract’.⁵² In a later discussion, Berg persuasively comments that reconstruction of the ‘background’ can be expensive, painstaking, or even impossible, when the ‘parties’ are complex organisations represented by legal and other professional ‘teams’, and the parties’ successors are now required retrospectively and minutely to examine the

48 [1997] AC 313, 388, HL.

49 *New Hampshire Insurance Co. v. MGN Ltd*, *The Times*, 25 July 1995, CA; *Scottish Power plc v. Britoil (Exploration) plc*, *The Times*, 2 December 1997, CA; Staughton, [1999] CLJ 303.

50 Sir Gavin Lightman, ‘Civil Litigation in the Twenty-First Century’ (1998) 17 *Civil Justice Quarterly* 373; similarly, E. McKendrick, in S. Worthington (ed.), *Commercial Law and Commercial Practice* (Oxford, 2003) 139, 147.

51 Gavin Lightman, ‘Civil Litigation in the Twenty-First Century’ (1998) 17 *Civil Justice Quarterly* 373; E. McKendrick, in S. Worthington (ed.), *Commercial Law and Commercial Practice* (Oxford, 2003) 139, 147.

52 A. Berg, (2006) 122 LQR 354, 362.

transaction's pre-formation landscape in order to capture its tacit nuances.⁵³ Berg notes the Chief Justice of New South Wales' condemnation of Lord Hoffmann's 'background' principle: '[I]t is not a schema that can be applied to a substantial range of commercial contractual relationships.'⁵⁴

- 14.11 However, Lord Hoffmann in the *BCCI* case (2001) tried to allay such fears.⁵⁵ He said that the courts should not encourage an uncontrolled 'trawl' through all background material.
- 14.12 There are three grounds for optimism. First, there is the possibility (as noted in the last two sentences of 14.03) of making a decision on a disputed point of interpretation during a summary hearing, under CPR Part 24, without waiting for witness evidence to be presented at trial. Secondly, Arden LJ in the *Egan* case (2004) has suggested that the CPR system of case management 'could obviously be used to keep evidence within proper bounds'.⁵⁶ For this reason, Arden LJ in *Square Mile Partnership Ltd v. Fitzmaurice McCall Ltd* (2006) criticised the first instance judge for failing to take control in this respect.⁵⁷ Thirdly, the Supreme Court's decision in the *Sigma* case (2009)⁵⁸ has suggested that the courts will not permit too deep a delving into background material unless that information was (to quote Lord Hoffmann's own formulation in the *Investors Compensation Scheme* case (1998), cited at 14.07) 'the background knowledge which would reasonably have been available to the parties in the situation in which they were at the time of the contract'. In the *Sigma* case, the Supreme Court construed a clause in a complex commercial document so as to reflect the overall structure of the document, eschewing a 'natural meaning' or literal construction of the particular clause in issue. In essence, therefore, the case turned on the need to interpret ambiguous language by reference to the whole document: 'the words must be set in the [internal] landscape of the instrument as a whole' (Lord Mance, quoting Lord Mustill in the *Charter Reinsurance* case (1997)).⁵⁹ Of great importance are the remarks by Lord Collins in the *Sigma* case (with whom Lords Mance and Hope agreed). Lord Collins emphatically disapproved⁶⁰ too broad a search for background information when, as in this case, the parties to the relevant transaction

53 A. Berg, (2008) 124 LQR 6, 12–14.

54 *Ibid.*, at 14, citing an address given by this Australian judge in March 2007.

55 [2001] 1 AC 251, at [39], HL.

56 *Egan v. Static Control Components (Europe) Ltd* [2004] EWCA Civ 392; [2004] 2 Lloyd's Rep 429; G. McMeel, *The Construction of Contracts* (Oxford, 2007), 1.67.

57 [2006] EWCA Civ 1690; [2007] 2 BCLC 23, at [76].

58 *In Re Sigma Finance Corporation (in administrative receivership)* [2009] UKSC 2; [2010] 1 All ER 571; [2010] BCC 40 (the Supreme Court's decision upholds the dissenting opinion of Lord Neuberger MR in the Court of Appeal, although he had candidly admitted that his solution to the riddle of the complex contract was one which had been 'spotted' by him only after the conclusion of oral argument on appeal: [2008] EWCA Civ 1303, at [134]). The *Sigma* case was briefly noted by Thomas LJ in *Royal Bank of Scotland plc v. Highland Financial Partners LP* [2010] EWCA Civ 809, at [11].

59 *In Re Sigma Finance Corporation (in administrative receivership)* [2009] UKSC 2; [2010] 1 All ER 571; [2010] BCC 40, at [9] (quoting Lord Mustill in *Charter Reinsurance Co. Ltd v. Fagan* [1997] AC 313, 384, HL).

60 *In Re Sigma Finance Corporation (in administrative receivership)* [2009] UKSC 2; [2010] 1 All ER 571; [2010] BCC 40, at [35] to [37].

might not have been present at its birth, and had instead become second-hand or remoter recipients of others' contractual text which had been in circulation in the relevant financial market:

Sigma financed its investments over a 13 year period by debt securities issued or guaranteed by it. It entered into liquidity facilities intended to hedge against market liquidity risks. It entered into financial instruments intended to hedge against currency and interest rate risk. Others provided liquidity facilities, or entered into financial hedging instruments. The Security Trust Deed secures a variety of creditors, who hold different instruments, issued at different times, and in different circumstances. Consequently this is not the type of case where the background or matrix of fact is or ought to be relevant, except in the most generalised way. I do not consider, therefore, that there is much assistance to be derived from the principles of interpretation re-stated by Lord Hoffmann in the familiar passage in the *Investors Compensation Scheme* case, 1998 [cited at 14.07 above]. Where a security document secures a number of creditors who have advanced funds over a long period it would be quite wrong to take account of circumstances which are not known to all of them. In this type of case it is the wording of the instrument which is paramount. The instrument must be interpreted as a whole in light of the commercial intention which may be inferred from the face of the instrument and from the nature of the debtor's business. Detailed semantic analysis must give way to business common sense: *The Antaios* [1985] AC 191, 201, HL.

4. THE PRE-CONTRACTUAL NEGOTIATION BAR⁶¹

- 14.13 Lord Wilberforce in *Prenn v. Simmonds* (1971) endorsed this long-standing 'bar'. It is applicable both to pre-contractual negotiations and to pre-contractual unilateral assumptions concerning the proposed text's meaning. He said:⁶²

[S]uch evidence is unhelpful. By the nature of things, where negotiations are difficult, the parties' positions, with each passing letter, are changing and until the final agreement, though converging, still divergent. It is only the final document which records a consensus.⁶³

Far more, and indeed totally, dangerous is to admit evidence of one party's objective – even if this is known to the other party. However strongly pursued this may be, the other party may only be willing to give it partial recognition, and in a world of give and take, men often have to be satisfied with less than they want. So, again, it would be a matter of speculation how far the common intention was that the particular objective should be realised ... [E]vidence of negotiations, or of the parties'

61 G. McMeel, *The Construction of Contracts* (Oxford, 2007), 5.77 ff; earlier, (2003) 119 LQR 272.

62 [1971] 1 WLR 1381, HL; in *Chartbrook Ltd v. Persimmon Homes Ltd* [2009] UKHL 38; [2009] 1 AC 1101, at [3] ff, [28] ff, Lords Hope and Hoffmann noted that the *Prenn* case had affirmed *Inglis v. John Buttery & Co.* (1878) 3 App Cas 552, 577, HL, Lord Blackburn (see the quotation in the present paragraph, below).

63 [1971] 1 WLR 1381, at 1384G.

intentions, and *a fortiori* [one party's] intentions, ought not to be received, and evidence should be restricted to evidence of the factual background known to the parties at or before the date of the contract, including evidence of the 'genesis' and objectively the 'aim' of the transaction.⁶⁴

14.14 The House of Lords in *Chartbrook Ltd v. Persimmon Homes Ltd* (2009)⁶⁵ retained this bar upon considering prior negotiations. Lord Hoffmann said:⁶⁶

The rule may well mean ... that parties are sometimes held bound by a contract in terms which, upon a full investigation of the course of negotiations, a reasonable observer would not have taken them to have intended. But a system which sometimes allows this to happen may be justified in the more general interest of economy and predictability in obtaining advice and adjudicating disputes. It is, after all, usually possible to avoid surprises by carefully reading the documents before signing them and there are the safety nets of rectification and estoppel by convention.

Lord Hoffmann noted Lord Blackburn's adoption in 1878 of the following statement by Lord Gifford, a Scottish judge, in 1877:⁶⁷

The very purpose of a formal contract is to put an end to the disputes which would inevitably arise if the matter were left upon verbal negotiations or upon mixed communications partly consisting of letters and partly of conversations. The written contract is that which is to be appealed to by both parties, however different it may be from their previous demands or stipulations, whether contained in letters or in verbal conversation.

In the *Chartbrook* case (2009), Lord Rodger added:⁶⁸

[T]here are no particular pressing circumstances which call for a change. The House is simply being asked to make a fresh policy decision and, in effect, to legislate to provide for a different rule. The wisdom of the proposed change is, however, debatable. So, if there is to be a change, it should be on the basis of a fully informed debate in a forum where the competing policies can be properly investigated and evaluated.

14.15 *Reasons for the bar upon admission of pre-contractual negotiations.*⁶⁹ At first instance in *Chartbrook Ltd v. Persimmon Homes Ltd* (2007), Briggs J,⁷⁰ drawing upon Lord Nicholls' 'My Kingdom for a Horse' lecture,⁷¹ identified four 'policy reasons' supporting this

64 *Ibid.*, at 1385C and 1385H.

65 [2009] UKHL 38; [2009] 1 AC 1101; noted by D. McLaughlan, (2010) 126 LQR 8–14.

66 *Ibid.*, at [41].

67 *Ibid.*, at [29], citing Lord Blackburn in *Inglis v. John Buttery & Co.* (1878) 3 App Cas 552, 577, HL, adopting Lord Gifford in the *Inglis* case (1877) 4 R 58, 69–70.

68 [2009] UKHL 38; [2009] 1 AC 1101, at [70].

69 In his note on the House of Lords decision in the *Chartbrook* case, D. McLaughlan, (2010) 126 LQR 8, 9–11, rejects these various suggested justifications.

70 [2007] EWHC 409 (Ch), at [23].

71 Lord Nicholls, 'My Kingdom for a Horse: The Meaning of Words' (2005) 121 LQR 577.

bar, namely: '(1) Increased uncertainty and unpredictability in dispute resolution; (2) Adverse effect on third party rights; (3) The use of the evidence would be "unhelpful", (4) Subversion of the objective approach.' In the Court of Appeal (2008),⁷² Lawrence Collins LJ added a fifth possible rationale for the same bar: (5) 'without such a rule sophisticated and knowledgeable negotiators would be tempted to lay a paper trail of self-serving documents.'⁷³ At first instance in this case, Briggs J had regarded point (2), 'adverse effect on third parties', as 'compelling'. However, when the case reached the Court of Appeal (2008),⁷⁴ Lawrence Collins LJ was unpersuaded that the 'third party impact' objection was powerful enough to justify the present 'bar',⁷⁵ and, in the House of Lords (2009) in the same case, Lord Hoffmann gave reasons for supporting Collins LJ's scepticism.⁷⁶ Lord Hoffmann placed emphasis on the other four arguments, especially the first argument concerning uncertainty and unpredictability. The following extracts from his judgment in the House of Lords provide cogent support for the exclusionary rule:⁷⁷

It reflects what may be a sound practical intuition that the law of contract is an institution designed to enforce promises with a high degree of predictability and that the more one allows conventional meanings or syntax to be displaced by inferences drawn from background, the less predictable the outcome is likely to be ...

[P]re-contractual negotiations seem to me capable of raising practical questions different from those created by other forms of background. Whereas the surrounding circumstances are, by definition, objective facts, which will usually be uncontroversial, statements in the course of pre-contractual negotiations will be drenched in subjectivity and may, if oral, be very much in dispute. It is often not easy to distinguish between those statements which (if they were made at all) merely reflect the aspirations of one or other of the parties and those which embody at least a provisional consensus which may throw light on the meaning of the contract which was eventually concluded. But the imprecision of the line between negotiation and provisional agreement is the very reason why in every case of dispute over interpretation, one or other of the parties is likely to require a court or arbitrator to take the course of negotiations into account.

- 14.16 Different approach in other jurisdictions.** Finally, how does English contractual interpretation compare with that employed or recommended elsewhere? McKendrick draws attention to the contrast between the English exclusionary rules of interpretation (barring reference to negotiations and post-formation conduct) and the liberal styles of interpretation espoused by PECL, the *Principles of European Contract Law*. That 'soft law'

⁷² [2008] EWCA Civ 183; [2008] 2 All ER (Comm) 387.

⁷³ *Ibid.*, at [111], *per* Lawrence Collins LJ; this argument is described as unconvincing by D. McLaughlan, (2010) 126 LQR 8, 11.

⁷⁴ [2008] EWCA Civ 183; [2008] 2 All ER (Comm) 387.

⁷⁵ *Ibid.*, at [112], *per* Lawrence Collins LJ.

⁷⁶ [2009] UKHL 38; [2009] 1 AC 1101, at [40].

⁷⁷ *Ibid.*, at [37], *per* Lord Hoffmann.

code is heavily influenced by civilian methods. It permits the court to have regard to a wide range of factors, including good faith and the Janus-like perspectives of pre- and post-formation dealings⁷⁸ (similarly, UNIDROIT's *Principles of International Commercial Contracts* (2004), Article 4.3,⁷⁹ permits a similarly wide range of matters to be taken into account; see also 21.02). Furthermore, the Dubai International Financial Centre's codification of English contract law permits such pre-formation and post-formation references (Article 51).⁸⁰ Furthermore, Lawrence Collins LJ in the Court of Appeal in *Chartbrook Ltd v. Persimmon Homes Ltd* (2008) noted that, in the USA, there is some support (although not unanimous) for courts referring to negotiations when construing written agreements if they conspicuously lack clarity.⁸¹

The reasons for the exclusionary rule are by no means self-evident. The American Law Institute, *Restatement Second: Contracts*, section 214, states that 'negotiations prior to ... the adoption of a writing are admissible in evidence to establish ... the meaning of the writing ...'. In the United States, contract law is generally a matter of State law, and the courts of the majority of States retain the 'plain meaning rule', namely that where the meaning of the language taken in context is clear, evidence of prior negotiations cannot be used in its interpretation. But there is a division of authority as to whether evidence of prior negotiations can be used to show whether contract language lacks the required degree of clarity: *Pacific Gas and Electric Co. v. GW Thomas Drayage and Rigging Co.*, 442 P 2d 641 (Cal. 1968); Farnsworth, *Contracts*, 4th edn, 2004, para. 7.12 [and] *Williston on Contracts* (4th edn, 2007, Lord), Vol. 11, para. 33.42.

Also in the *Chartbrook* case, in the House of Lords (2009),⁸² Lord Hoffmann considered the different approaches of English law and 'soft law' codes influenced by civilian ideas:⁸³

Both the UNIDROIT *Principles of International Commercial Contracts* (1994 and 2004 revision)⁸⁴ [21.02] and the *Principles of European Contract Law* (1999) provide that in ascertaining the 'common intention of the parties', regard shall be had to

78 E. McKendrick, in S. Worthington (ed.), *Commercial Law and Commercial Practice* (Oxford, 2003), 139, 161–2, noting *Principles of European Contract Law*, Article 5:102 (a)(b) and (g).

79 2nd edn, Rome, 2004; see M. J. Bonell (ed.), *The UNIDROIT Principles in Practice: Case Law and Bibliography on the UNIDROIT Principles of International Commercial Contracts* (2nd edn, Ardsley, NY, 2006), 234 ff; S. Vogenauer and J. Kleinheisterkamp (eds.), *Commentary on the UNIDROIT Principles of International Commercial Contracts* (Oxford, 2009), 510 ff.

80 Available at www.difc.ae/laws-regulations/ (Dubai International Financial Centre).

81 [2008] EWCA Civ 183; [2008] 2 All ER (Comm) 387, at [108] to [113], *per* Lawrence Collins LJ.

82 [2009] UKHL 38; [2009] 1 AC 1101; noted by D. McLaughlan (2010) 126 LQR 8–14.

83 *Ibid.*, at [39].

84 2nd edn, Rome, 2004; see M. J. Bonell (ed.), *The UNIDROIT Principles in Practice: Case Law and Bibliography on the UNIDROIT Principles of International Commercial Contracts* (2nd edn, Ardsley, NY, 2006), 234 ff; S. Vogenauer and J. Kleinheisterkamp (eds.), *Commentary on the UNIDROIT Principles of International Commercial Contracts* (Oxford, 2009), 510 ff; M. J. Bonell, 'The UNIDROIT Principles and CISG – Sources of Inspiration for English Courts?' [2006] 11 *Uniform Law Review* 305, who cites *Gloster J in Svenska Petroleum Exploration AB v. Government of the Republic of Lithuania* (No. 2) [2005] EWHC 2437 (Comm); [2006] 1 All ER (Comm) 731, at [80] ff and 99 ff (discussion of foreign interpretative methods at [23] ff).

prior negotiations: articles 4.3 and 5.102 respectively. The same is true of the United Nations Convention on Contracts for the International Sale of Goods (1980).

But these instruments reflect the French philosophy of contractual interpretation, which is altogether different from that of English law. As Professor Catherine Valcke⁸⁵ explains in an illuminating article ('On Comparing French and English Contract Law: Insights from Social Contract Theory') (16 January 2009), French law regards the intentions of the parties as a pure question of subjective fact, their *volonté psychologique*, uninfluenced by any rules of law.

It follows that any evidence of what they said or did, whether to each other or to third parties, may be relevant to establishing what their intentions actually were.

There is in French law a sharp distinction between the ascertainment of their intentions and the application of legal rules which may, in the interests of fairness to other parties or otherwise, limit the extent to which those intentions are given effect. English law, on the other hand, mixes up the ascertainment of intention with the rules of law by depersonalising the contracting parties and asking, not what their intentions actually were, but what a reasonable outside observer would have taken them to be.

One cannot in my opinion simply transpose rules based on one philosophy of contractual interpretation to another, or assume that the practical effect of admitting such evidence under the English system of civil procedure will be the same as that under a Continental system.

In fact, as Eric Clive has noted, the capacity of a party to plead rectification and thus, for the purpose of that equitable doctrine, to gain access to pre-contractual negotiations (14.38), means that in many English trials the judge does discover details of the pre-contractual negotiations: and, to this extent, the doctrinal contrast between English law and civilian systems is a matter of no great practical significance.⁸⁶

- 14.17 *Rejection in Chartbrook (2009) of the 'private dictionary' exception to the pre-contractual negotiation bar.* In *'The Karen Oltmann'* (1976),⁸⁷ Kerr J had appeared to carve out a wide exception to the exclusion bar upon pre-contractual discussion. Such extrinsic evidence would be admitted, in his view, for the purpose of showing that the parties *had agreed on how a particular word or phrase would be understood by them*. This became known as the

85 See also C. Valcke, 'Contractual Interpretation at Common Law and Civil Law: An Exercise in Comparative Legal Rhetoric', in J. W. Neyers, R. Bronaugh and S. G. A. Pitel (eds.), *Exploring Contract Law* (Oxford, 2009), 77 ff.

86 E. Clive, in H. MacQueen and R. Zimmermann (eds.), *European Contract Law: Scots and South African Perspectives* (Edinburgh, 2006), chapter 7, at 183.

87 [1976] 2 Lloyds Rep 708, 712, 713, Kerr J.

'private dictionary' exception to the general bar. In *'The Karen Oltmann'* (1976),⁸⁸ Kerr J fortified his interpretation of 'first impression' by referring to the parties' negotiations, taking the view that this was permitted because those discussions indicated a consensual resolution of an ambiguous word.

Kerr J had to construe the word 'after', which appeared in a break clause. The agreement stated: 'Charterers to have the option to redeliver the vessel after 12 months' trading subject giving 3 months' notice.' Kerr J held as a matter of first impression that the word 'after' had been used in the sense of 'on the expiry of' and not in the sense of 'at any time after the expiry of'. He fortified this by referring to the parties' negotiations. From these he discovered that this was indeed the agreed basis on which the word 'after' had been used. Kerr J held:⁸⁹

If a contract contains words which, in their context, are fairly capable of bearing more than one meaning, and if it is alleged that the parties have in effect negotiated on an agreed basis that the words bore only one of the two possible meanings, then it is permissible for the court to examine the extrinsic evidence relied upon to see whether the parties have in fact used the words in question in one sense only, so that they have in effect given their own dictionary meaning to the words as the result of their common intention.

14.18 However, Lawrence Collins LJ in *Chartbrook Ltd v. Persimmon Homes Ltd* (2008)⁹⁰ expressed doubts whether this exception is appropriate.

14.19 Then, Kerr J's suggested exception was formally repudiated by Lord Hoffmann in the House of Lords in the *Chartbrook* case (2009), who condemned Kerr J's approach as a voracious exception capable of swallowing the main rule:⁹¹

On its facts, *'The Karen Oltmann'* was in my opinion an illegitimate extension of the 'private dictionary' principle which, taken to its logical conclusion, would destroy the exclusionary rule and any practical advantages which it may have.

14.20 However, in the *Chartbrook* case (2009), Lord Hoffmann noted that it is acceptable to adduce extrinsic evidence in the following three situations, each of which will continue to be troublesome, for they are in truth three large holes in the general doctrine which purports to exclude reference to pre-contractual negotiations.

- (1) The first exception arises where a party wishes to show (if necessary, by reference to the parties' negotiations) that the contract contains words or phrases that have been used in a quite unusual sense by the parties in a course of dealing or that they are used in a special sense by members of a particular trade or sect. On this exception, Lord Hoffmann said in the *Chartbrook* case (2009):⁹²

⁸⁸ [1976] 2 Lloyd's Rep 708, 712, 713, Kerr J.

⁸⁹ *Ibid.*, at 712.

⁹⁰ [2008] EWCA Civ 183; [2008] 2 All ER (Comm) 387.

⁹¹ [2009] UKHL 38; [2009] 1 AC 1101, at [47].

⁹² [2009] UKHL 38; [2009] 1 AC 1101, at [45].

[E]vidence may always be adduced that the parties habitually used words in an unconventional sense in order to support an argument that words in a contract should bear a similar unconventional meaning. This is ... akin to the principle by which a linguistic usage in a trade or among a religious sect may be proved: compare *Shore v. Wilson* (1842) 9 Cl & F 355. For this purpose it does not matter whether the evidence of usage by the parties was in the course of negotiations or on any other occasion. It is simply evidence of the linguistic usage which they had in common.

However, McLaughlan⁹³ has rightly suggested that this qualification is troublesome because there is no workable distinction between an 'unusual' meaning and a choice between more than one 'ordinary' meanings.

As for the next two exceptions, it will be convenient first to quote from Lord Hoffmann's speech in the *Chartbrook* case (2009)⁹⁴ (more generally on rectification, see 14.33 ff below):

There are two [further] legitimate safety devices which will in most cases prevent the exclusionary rule from causing injustice. But they have to be specifically pleaded and clearly established. One is rectification. The other is estoppel by convention ... If the parties have negotiated an agreement upon some common assumption, which may include an assumption that certain words will bear a certain meaning, they may be estopped from contending that the words should be given a different meaning. Both of these remedies lie outside the exclusionary rule, since they start from the premise that, as a matter of construction, the agreement does not have the meaning for which the party seeking rectification or raising an estoppel contends.

- (2) The second exception arises where the parties have outwardly reached an agreement concerning words in the written contract so that each is estopped from denying the non-literal construction which they wish to place on those words. This is 'estoppel by convention' (5.68). To establish estoppel by convention, an implicit agreement must be manifested in the parties' pattern of behaviour and interaction. In *Amalgamated Investment & Property Co. Ltd v. Texas Commerce International Bank Ltd* (1982), Lord Denning MR explained: 'It is available – not so as to construe the contract – but to see how they themselves acted on it. Under the guise of estoppel [by convention] we can prevent either party from going back on the interpretation they themselves gave to it.'⁹⁵ Aikens J found such an estoppel by convention in *Harper v. Interchange Group Ltd* (2007),⁹⁶ but then decided that nothing significant had occurred to make it unconscionable for the provisionally estopped party to insist on the original terms of the contract. Unless category (2) is restricted to

⁹³ D. McLaughlan, (2010) 126 LQR 8, 12 (case note).

⁹⁴ [2009] UKHL 38; [2009] 1 AC 1101, at [47].

⁹⁵ [1982] QB 84, 120, CA.

⁹⁶ [2007] EWHC 1834 (Comm), at [133] ff.

post-formation dealings, it will involve the same vice as that condemned by Lord Hoffmann when repudiating the ‘private dictionary’ doctrine (namely, a tendency for an exception to eat up the main rule: 14.19). However, his reference to this doctrine does not appear to restrict the focus to post-formation dealings, because he said: ‘[I]f the parties have negotiated an agreement upon some common assumption, which may include an assumption that certain words will bear a certain meaning, they may be estopped from contending that the words should be given a different meaning.’⁹⁷

- (3) A third exception concerns the scope for rectifying an agreement to ensure that it accurately reflects the outward consensus that the parties had reached (14.33 ff). This third qualification involves reference to pre-formation negotiations. It is consistently invoked as a means of requiring the court to consider pre-formation negotiations.

5. ‘INTERPRETATION’ TO ELIMINATE OBVIOUS OR DEMONSTRABLE ERRORS

- 14.21 The court can ‘construe’ a document, if necessary by radical rewriting, when it is obvious from the existing text that a drafting or clerical error has corrupted or bungled the final text, or at least such a textual problem is demonstrable when that text is read against its commercial context and with regard to the transaction’s aim. In principle, the process of adding words to a text, or removing them, should be different from interpreting the text by giving meaning to words contained in the text. However, as Burrows notes,⁹⁸ this liberal style of modern ‘interpretation’ has eroded this distinction between textual emendation and exegesis (that is, elucidation, or making sense, of a ‘stable’ text). This includes the possibility of ‘reading in’ words or ‘substituting’ words or whole phrases in a manifestly defective text. Leading examples of ‘reconstitutive interpretation’ will be noted at 14.23 and 14.24.⁹⁹ This style of ‘interpretation’ has a similar function to the more formal equitable doctrine of ‘rectification’ (14.33 ff): both doctrines have the effect of revising a document. The revised form takes effect from the date when the document took legal effect. The safer course is to plead both ‘construction’ and ‘rectification’ (and litigation lawyers frequently do this). The ‘pre-contractual negotiation’ bar prohibits reference to evidence of the parties’ negotiations if the claim is founded on common law ‘construction’ (but see the three qualifications explained at 14.20); whereas, an equitable claim for rectification is an established exception to this restriction. (Sir Richard Buxton, a former Lord Justice of Appeal, has suggested (1) that reconstitutive interpretation is an ill-conceived innovation of

⁹⁷ [2009] UKHL 38; [2009] 1 AC 1101, at [47].

⁹⁸ A. Burrows, ‘Construction and Rectification’, in A. Burrows and E. Peel (eds.), *Contract Terms* (Oxford, 2007), 77, 79 n. 9.

⁹⁹ *Holding & Barnes plc v. Hill House Hammond Ltd* (No. 1) [2001] EWCA Civ 1334; [2002] L & TR 103 (14.24); *Littman v. Aspen Oil (Broking) Ltd* [2005] EWCA Civ 1579 (14.24); see also *The Starsin* [2004] 1 AC 715, HL; noted by E. Peel, (2004) 120 LQR 11–16. Contrast *William Hare v. Shepherd* [2010] EWCA Civ 283.

the *Investors Compensation Scheme* ‘restatement’, and (2) that rectification should be the sole legal technique available to recast the text of the written contract. Buxton’s 2010 article was cited by the Supreme Court in *Oceanbulk Shipping and Trading SA v. TMT Asia Ltd* (2010),¹⁰⁰ but Lord Clarke distanced himself from proposition (2), just summarised.)

- 14.22 *Chartbrook* (2009): clarification of the requirements of reconstitutive interpretation. *Chartbrook Ltd v. Persimmon Homes Ltd* (2009)¹⁰¹ concerned an ‘overage’ (or ‘clawback’) clause in an urban development agreement under which the owners, Chartbrook, had claimed extra payment. Chartbrook’s interpretation had been preferred both by Briggs J and the Court of Appeal (Lawrence Collins LJ dissenting). However, the developer, Persimmon, won (convincingly) in the House of Lords. Three main points emerge from the decision. First, the House of Lords affirmed the exclusionary rule prohibiting reference to the parties’ negotiations as an aid to the interpretation of written contracts, subject to exceptions of the doctrine of estoppel by convention (14.20, 5.68) and the equitable principle of rectification (14.33 ff); and rejected Kerr J’s ‘private dictionary’, or special prior meaning, exception to that rule (*The Karen Oltmann*’ (1976)) (14.17 to 14.19).¹⁰² Secondly, the *Chartbrook* case contains observations on rectification and its relationship with the process of interpretation (14.33 ff). Thirdly, the House of Lords confirmed the courts’ capacity to ‘cure’ defective drafting by reference to the contract’s background, genesis and aim, and this can involve extensive reconstruction of botched drafting, provided a reasonable third party can clearly and objectively discern the parties’ shared intended meaning.¹⁰³ Lord Hoffmann said:¹⁰⁴ ‘[T]here is not, so to speak, a limit to the amount of red ink or verbal rearrangement or correction which the court is allowed.’ This is a widely expressed invitation to potential litigants to contest matters of interpretation, and it seems destined to stimulate much litigation.¹⁰⁵ Lord Hoffmann summarised the governing principles as follows:¹⁰⁶

In *East v. Pantiles (Plant Hire)* (1981), Brightman J stated the conditions for what he called ‘correction of mistakes by construction’: ‘first, there must be a clear mistake on the face of the instrument; secondly, it must be clear what correction ought to be made in order to cure the mistake. If those conditions are satisfied, then the correction is made as a matter of construction.’ [This is now] subject to two qualifications, both of which are explained by Carnwath LJ in ... *KPMG LLP v. Network Rail*

100 [2010] UKSC 44; [2010] 3 WLR 1424, at [45], first sentence.

101 [2009] UKHL 38; [2009] 1 AC 1101.

102 [1976] 2 Lloyds Rep 708, 712, 713, Kerr J.

103 [2009] UKHL 38; [2009] 1 AC 1101, at [25].

104 *Ibid.*, at [25].

105 E.g. *Bishops Wholesale Newsagency Ltd v. Surridge Dawson Ltd* [2009] EWHC 2578 (Ch), Judge Mackie QC; *CDV Software Entertainment AG v. Gamecock Media Europe Ltd* [2009] EWHC 2965 (Ch), Gloster J; *Deutsche Bank AG v. Sebastian Holdings Inc.* [2009] EWHC 2132 (Comm), Walker J; *HHR Pascal BV v. W2005 Puppet II BV* [2009] EWHC 2771 (Comm); *NHS Business Services Authority v. Ingram* [2009] EWHC 2486 (Ch).

106 [2009] UKHL 38; [2009] 1 AC 1101, at [22] to [25].

Infrastructure Ltd (2007). The first qualification is that ‘correction of mistakes by construction’¹⁰⁷ is not a separate branch of the law ... As Carnwath LJ said:¹⁰⁸ ‘Both in the judgment, and in the arguments before us, there was a tendency to deal separately with correction of mistakes and construing the paragraph “as it stands”, as though they were distinct exercises. In my view, they are simply aspects of the single task of interpreting the agreement in its context, in order to get as close as possible to the meaning which the parties intended.’

Lord Hoffmann continued (in the *Chartbrook* case (2009)):¹⁰⁹

[In] deciding whether there is a clear mistake, the court is not confined to reading the document without regard to its background or context. As the exercise is part of the single task of interpretation, the background and context must always be taken into consideration.

- 14.23 *Disputed point of interpretation in the Chartbrook case.* The parties had agreed that Persimmon, the developer, would make a ‘minimum’ payment to Chartbrook, the owners: the so-called ‘Total Residential Land Value’. It would be calculated by reference to the floor area of the building for which planning permission for flats was granted. But the bone of contention concerned the possibility of a further payment: for it was also agreed that the developer *might* also have to pay an ‘Additional Residential Payment’ (ARP), defined as ‘23.4% of the price achieved for each Residential Unit in excess of the Minimum Guaranteed Residential Unit Value less the Costs and Incentives’. The owner’s (Chartbrook) version of ARP would produce an additional payment of £4,484,862, whereas Persimmon’s version of ARP would produce an additional payment of £897,051. Finding in favour of Persimmon, Lord Hoffmann concluded that the correct reconstruction of the ARP must be this:¹¹⁰ ‘You deduct the C & I from the ... [actual] price achieved [by sales of the long leases of the 100 flats to third parties]’ and then ‘the [total] ARP [for the whole residential site] is the excess, if any, of 23.4% of that net sum over the [Total Residential Land Value]’. The following points were the ‘telling factors’ which operated in favour of Persimmon’s suggested construction. First, there were *internal clues*: the first payment, the Minimum Guaranteed Residential Unit Value, was explicitly a ‘*minimum guaranteed*’ sum, and so, by clear implication, the supplementary payment, the ARP, was not guaranteed, but a *possible* extra sum.¹¹¹ Secondly, there was the *commercial background and transaction’s aim*: Chartbrook’s interpretation would entitle them to substantial amounts of ARP, even if the flats were

107 [2007] EWCA Civ 363; [2007] Bus LR 1336.

108 [2009] UKHL 38; [2009] 1 AC 1101, at [50].

109 *Ibid.*, at [24].

110 As for these terms: ‘Residential Unit’ meant a flat; ‘Minimum Guaranteed Residential Unit Value’ (‘MGRUV’) meant the Total Residential Land Value divided by the number of flats (100); ‘Costs and Incentives’ (‘C & I’) meant the additional expense which Persimmon might incur to entice buyers, for example, by providing fittings better than specification or paying legal expenses.

111 *Ibid.*, at [16] and [17].

sold at sums greatly below the anticipated figure of c £200,000.¹¹² Thirdly, the presence of a concurrent claim to rectification enabled the court in this litigation (including the House of Lords) to have a ‘legitimate peep’ at the relevant negotiations and so check that Persimmon’s proposed terms, provisionally accepted by Chartbrook, were structured in the way just summarised (during a rectification claim, a party is permitted to adduce extrinsic oral or written evidence to determine their pre-contractual intentions and negotiations: 14.38).

- 14.24 *Further illustrations of reconstitutive interpretation.*¹¹³ Besides the *Chartbrook* case itself (14.23), the pre-*Chartbrook* case law (approved by the House of Lords in that case) contains helpful illustrations of this style of interpretation. Each of the following Court of Appeal decisions concerned botched clauses within commercial leases: *Holding & Barnes plc v. Hill House Hammond Ltd (No. 1)* (2001);¹¹⁴ *Littman v. Aspen Oil (Broking) Ltd* (2005);¹¹⁵ and *KPMG LLP v. Network Rail Infrastructure Ltd* (2007).¹¹⁶ For reasons of space, only the *Littmann* case will be summarised here.

In *Littman v. Aspen Oil (Broking) Ltd* (2005),¹¹⁷ a lease contained a mutual break clause exercisable by either party upon giving six months’ written notice. The landlord had intended that the contract should permit the tenant to exercise this break clause only if the tenant had complied with its covenants at the relevant time. But the botched text stated:

that up to the Termination Date in the case of a notice *given by the Landlord* the Tenant shall have paid the rents ... and shall have duly observed and performed the Tenant’s covenants ... and the conditions herein contained.

The highlighted words were the source of the problem. The Court of Appeal upheld Hart J’s decision that the words highlighted above should be construed to read: ‘given by the Tenant’. There is no need for the corrupted text to be grammatically or syntactically wrong. Such ‘construction’ could cure a manifest slip. Otherwise, the final text would be commercial nonsense.

- 14.25 In the final three sections of this chapter, we will look at three connected doctrines: the parol evidence rule (14.26); implication of terms in the context of written contracts (14.32); and the equitable doctrine of rectification (14.33).

112 *Ibid.*, at [18], [19] and [26].

113 Similarly, *Dalkia Utilities Services plc v. Celtech International Ltd* [2006] EWHC 63 (Comm); [2006] 1 Lloyd’s Rep 599, at [119].

114 [2001] EWCA Civ 1334; [2002] L & TR 103.

115 [2005] EWCA Civ 1579.

116 [2007] EWCA Civ 363; [2007] Bus LR 1336.

117 [2005] EWCA Civ 1579; upholding [2005] EWHC 1369 (Ch), Hart J.

6. INTERPRETATION AND THE PAROL EVIDENCE RULE¹¹⁸

- 14.26 This rule applies if a contract is wholly contained in writing. It does not apply if the contract is only partly written and partly oral.¹¹⁹ The rule prevents a party resorting to outside oral or written evidence *to add to, subtract from, vary or contradict* the written terms; and so a party cannot for this purpose give oral evidence of what he or even both parties intended, nor refer to drafts or other aspects of the negotiation. It is submitted that (1) the parol evidence rule is best understood, as formulated above, as concerned with the addition, subtraction, etc. of words; and this rule is different from (2) the now abrogated 'best evidence' rule (the need to produce an original document; a rule now excised from civil law)¹²⁰ and from (3) the exclusionary rule barring reference to pre-formation communications for the purpose of interpreting contractual written language.¹²¹
- 14.27 There are five reasons supporting the parol evidence rule: (1) reference to outside material or oral statements would complicate and unsettle the process of discovering the agreement's meaning and effect; (2) it is notorious that some negotiations involve rapid and not always transparent shifts of position;¹²² (3) the rule acknowledges that only the final written version of the contract counts; the parties should be expected to check and double-check the final document; (4) third parties might have innocently relied upon the document; but they are unlikely to have been privy to the parties' prior negotiations;¹²³ and (5) if the rule did not exist, parties might be tempted to manufacture 'self-serving' declarations of their preferred interpretation during the negotiations.
- 14.28 There are four qualifications upon (or circumventions of) the parol evidence rule. First, there is the doctrine of *rectification* (14.33 ff). Secondly, *collateral warranties*, normally based on oral assurances, are treated as free-standing agreements (9.05 to 9.10). Formally, therefore, collateral warranties do not violate the parol evidence rule, which is concerned only with the integrity of the written agreement. That rule does not prohibit proof of additional and free-standing contracts.¹²⁴ It is common for commercial agreements to contain an 'entire agreement' clause to exclude such side-agreements (9.27).¹²⁵ Thirdly,
- 118 *Chitty on Contracts* (30th edn, London, 2008), 12-096 ff; *Treitel* (12th edn, London, 2007), 6-012 ff; Law Commission, *The Law of Contract: The Parol Evidence Rule* (Law Commission Report No. 154, Cmnd 9700, London, 1986) (noted by G. Marston, [1986] CLJ 192); D. W. McLaughlan, *The Parol Evidence Rule* (1976); R. Stevens, 'Objectivity, Mistake and the Parol Evidence Rule', in A. Burrows and E. Peel (eds.), *Contract Terms* (Oxford, 2007), chapter 6, at 107 ff.
- 119 Law Commission, *The Law of Contract: The Parol Evidence Rule* (Law Commission Report No. 154, Cmnd 9700, London, 1986), 2.10, 2.11.
- 120 Rule now excised from English law following the *Springsteen* case, [2001] EWCA Civ 513; [2001] CPLR 369; [2001] EMLR 654, CA; N. Andrews, *English Civil Procedure* (Oxford, 2003), 31.29 ff; and G. McMeel, *The Construction of Contracts* (Oxford, 2007), 26.18 ff.
- 121 Cf the undifferentiated presentation of rules (1) to (3) in G. McMeel, *The Construction of Contracts* (Oxford, 2007), 5.30.
- 122 *Prenn v. Simonds* [1971] 1 WLR 1381, 1384, HL, per Lord Wilberforce.
- 123 Law Commission, *The Law of Contract: The Parol Evidence Rule* (Law Commission Report No. 154, Cmnd 9700, London, 1986), 2.43, on the position of assignees.
- 124 *Ibid.*, at 2.32 to 2.36.
- 125 *Chitty on Contracts* (30th edn, London, 2008), 12-104.

there are questions of *contractual invalidity*, etc. Extrinsic evidence is admissible to show that the supposed written contract is invalid, void, vitiated, or otherwise inoperative for any of these reasons: (1) mistake; (2) lack of consideration; (3) statutory non-compliance; (4) illegality; (5) fraud; (6) misrepresentation; (7) duress; (8) the agreement is subject to a condition precedent; and (9) the agreement has been subsequently varied or discharged by consensus. Fourthly, extrinsic evidence is admissible to show that it is one type of agreement (for example, a mortgage rather than a conveyance), or to reveal the identity of the parties, or to discover the subject matter of the agreement.¹²⁶

14.29 *Critique of the parol evidence rule.* On the one hand, the rule seems to stand for certainty, the integrity of an agreed text, and avoidance of side disputes. On the other hand, the rule yields to proof that the text is not in fact the exclusive source of contractual arrangements between the parties. For this reason some commentators take the radical view that this 'rule' is largely a mirage (most recently, McMeel),¹²⁷ contending that the supposed rule is easily displaced by adducing evidence that the ostensible written contract is not a free-standing agreement but an amalgam of written and oral undertakings (14.05), or that there is a separate 'collateral warranty' subsisting in parallel to the main written agreement (9.05 to 9.10).

14.30 However, in Treitel's opinion, the parol evidence rule creates a presumption that a contract in writing which *looks* like an agreement fixed in writing is indeed a complete agreement unless the party resisting that shows that the parties did not intend the agreement to be an exclusive statement of their relations.¹²⁸ Robert Stevens suggests that:

Once it is shown that the parties have agreed to be bound to the terms of a contract wholly embodied in a written instrument, each is bound by its terms although one or other might not know what they are, and even though the content of previous negotiations might be inconsistent with the terms contained in the contract ... Giving effect to different terms from those contained in the written agreement would be contrary to the agreement the parties have reached.¹²⁹

14.31 It is submitted that the parol evidence rule remains an important starting point in English contractual analysis. McMeel concedes that 'to date [this] rule has not been formally repudiated by higher courts'.¹³⁰ In fact, Lord Hobhouse 'saluted' this rule in the *Shogun* case (2003), describing it as 'one of the main reasons for the international success of English law'.¹³¹ He added:

¹²⁶ *Ibid.*, at 12-106 to 12-113, 12-122, 12-123.

¹²⁷ G. McMeel, *The Construction of Contracts* (Oxford, 2007), 5.24 ff, noting especially Law Commission, *The Law of Contract: The Parol Evidence Rule* (Law Commission Report No. 154, Cmnd 9700, London, 1986); *Chitty on Contracts* (30th edn, London, 2008), 12-096 ff; K. Wedderburn, 'Collateral Contracts' [1959] CLJ 58.

¹²⁸ Treitel (12th edn, London, 2007), 6-013.

¹²⁹ R. Stevens, in A. Burrows and E. Peel (eds.), *Contract Terms* (Oxford, 2007), 102, 107.

¹³⁰ G. McMeel, *The Construction of Contracts* (Oxford, 2007), 5.25.

¹³¹ *Shogun Finance Ltd v. Hudson* [2003] UKHL 62; [2004] 1 AC 919, HL, at [49], *per* Lord Hobhouse (see 10.31 ff for a detailed examination of this case); see also *Bank of Australasia v. Palmer* [1897] AC 540, 545, PC, *per* Lord Morris.

The relevant principle is well summarised in *Phipson on Evidence*:¹³² ‘When the parties have deliberately put their agreement into writing, it is conclusively presumed between themselves and their privies that they intend the writing to form a full and final statement of their intentions, and one which should be placed beyond the reach of future controversy, bad faith or treacherous memory.’

And in the context of interpretation of written contracts, and the exclusionary rule concerning pre-contractual negotiations (14.13 ff), Lord Hoffmann in *Chartbrook Ltd v. Persimmon Homes Ltd* (2009) said:¹³³

There is certainly a view in the profession that the less one has to resort to any form of background in aid of interpretation, the better. The document should so far as possible speak for itself. As Popham CJ said in the *Countess of Rutland’s Case* (1604) 5 Co Rep 25b, 26a: ‘it would be inconvenient, that matters in writing made by advice and on consideration, and which finally import the certain truth of the agreement of the parties should be controlled by averment of the parties to be proved by the uncertain testimony of slippery memory.’

7. INTERPRETATION AND IMPLIED TERMS¹³⁴

14.32 As explained at 13.01, there are three types of implied terms: (1) those implied by law (by statute, or by judicial decision); (2) those implied in fact; and (3) those implied on the basis of custom or trade usage.¹³⁵ The courts can imply a term into a written contract, but they will be slow to do so if the contract is closely drafted and made between parties of roughly equal bargaining power. This is explained at 13.15.

8. RECTIFICATION¹³⁶

14.33 The main propositions are:

- (1) A contract can be rectified to bring a written contract (or other ‘instrument’)¹³⁷ into conformity with the parties’ pre-contractual and shared understanding of its terms,

¹³² Now *Phipson on Evidence* (17th edn, 2009), chapter 42.

¹³³ [2009] UKHL 38; [2009] 1 AC 1101, at [36].

¹³⁴ On the connection between interpretation and implied terms, see G. McMeel, *The Construction of Contracts* (Oxford, 2007), 1.14 ff, and chapters 10–12.

¹³⁵ *Treitel* (12th edn, London, 2007), 8-064, citing cases concerning omission of customary terms from written contracts.

¹³⁶ *Butterworths Law of Contract* (3rd edn, London, 2007), 4.112 ff (in the section edited by M. A. Clarke); *Chitty on Contracts* (30th edn, London, 2008), 5-107 ff; R. Goff and G. H. Jones, *The Law of Restitution* (7th edn, London, 2007), 9-060 ff; *Meagher, Gummow and Lehane’s Equity: Doctrines and Remedies* (4th edn, Sydney, 2003), chapter 26; *Snell’s Principles of Equity* (31st edn, London, 2005), chapter 14; *Spry’s Equitable Remedies* (6th edn, Sydney, 2001), chapter 6; *Treitel* (12th edn, London, 2007), 8-059 ff; D. Wright, in P. Parkinson (ed.), *Principles of Equity* (Sydney, 1996), chapter 27; M. Smith, (2007) 123 LQR 116.

¹³⁷ Generally, see *Snell’s Principles of Equity* (31st edn, London, 2005), 14-06; ‘instrument’ includes, for example, nominations of pensions beneficiaries: *Collins v. Jones and Jones*, *The Times*, 3 February 2000

- provided: (a) there is some outward manifestation of that understanding;¹³⁸ and (b) the ‘understanding’ is ascertained and construed by resort to the objective method (14.35 on Lord Hoffmann’s discussion in the *Chartbrook* case (2009)).
- (2) There is no scope for rectification if both parties thought that they were dealing with subject matter ‘Y’, but they used the label ‘X’ throughout their dealings, and the written contract records the subject matter as ‘X’.¹³⁹
 - (3) Nor is rectification available to rectify one party’s mistake,¹⁴⁰ unless party B is aware that party A is mistaken concerning the contents or meaning of the written terms. In the latter situation, if B stays silent, B cannot take advantage of A’s mistake: the contract can be rectified in A’s favour.¹⁴¹ This is justified on the basis of B’s unconscionable acquiescence in A’s error.
 - (4) There are *dicta* that rectification in favour of A is also available if B creates a smoke-screen during negotiations and deflects attention from a certain clause (one which is favourable to B but not to A). B can deflect attention by concentrating the negotiations on other clauses; the elements of awareness and silence need not be shown in this situation (see (3) above). This extension of rectification to counter this form of guile is not settled and is controversial in principle.¹⁴²
 - (5) Rectification is an equitable remedy; therefore, it is a discretionary source of relief.¹⁴³
 - (6) When considering a claim for rectification, the court can admit extrinsic evidence: neither the exclusionary bar on pre-contractual negotiations (14.13 ff) nor the parol evidence rule (14.26 ff) will restrict the process of discerning the parties’ pre-contractual intentions and negotiations; nor, it seems, does an ‘entire agreement’ clause (9.27) preclude such an extrinsic search.¹⁴⁴
 - (7) The equitable doctrine of rectification need not be invoked if the court can, as a matter of simple ‘construction’, revise the relevant document. The latter is possible if: (a) it is clear that the present wording makes no commercial sense; and (b) it is apparent how the document should be reconstructed.¹⁴⁵ This aspect of construction

(Stanley Burnton QC); generally on rectification of voluntary settlements, see *Snell’s Principles of Equity* (31st edn, London, 2005), 14-07, and *Meagher, Gummow and Lehane’s Equity: Doctrines and Remedies* (4th edn, Sydney, 2003), 26-055 to 26-075 (but wills fell outside the ordinary law of rectification; section 20 of the Administration of Justice Act 1982 now adds a statutory species of (circumscribed) rectification: applied in *Re Segelman* [1996] Ch 171, 180 ff).

138 *Joscelyne v. Nissen* [1970] 2 QB 86, CA.

139 *Rose (Frederick E) (London) Ltd v. Wm H Pim Junr & Co. Ltd* [1953] 2 QB 450, CA.

140 *Riverlate Properties v. Paul* [1975] Ch 133, CA.

141 *Thomas Bates & Son Ltd v. Wyndham’s (Lingerie) Ltd* [1981] 1 WLR 505, CA.

142 *Commission for New Towns v. Cooper (GB) Ltd* [1995] Ch 259, CA.

143 On discretion in the context of voluntary settlements, see *Re Butlin’s Settlement* [1976] 1 Ch 251, 262, per Brightman J; *Sylvan Lake Golf & Tennis Club Ltd v. Performance Industries Ltd* (2002) 209 DLR (4th) 318 (Supreme Court of Canada), at [67] to [71].

144 *Chitty on Contracts* (30th edn, London, 2008), 5-112, citing *JJ Huber (Investments) v. Private DIY Co. Ltd* [1995] NPC 102.

145 *Holding & Barnes plc v. Hill House Hammond Ltd (No. 1)* [2001] EWCA Civ 1334; [2002] L & TR 103 (14.24); *Littman v. Aspen Oil (Broking) Ltd* [2005] EWCA Civ 1579 (14.24); and see *Nittan (UK) Ltd v. Solent Steel Fabrication Ltd* [1981] 1 Lloyd’s Rep 633, CA.

is examined at 14.21 ff. However, in practice, both techniques are frequently used as a 'double-barrelled' attack.

- (8) The doctrines of implied terms (chapter 13)¹⁴⁶ and estoppel by convention (14.06, 14.22 and 5.68)¹⁴⁷ can also overlap with rectification.

14.34 *Common intention error: general operation.* In *Swainland Builders Ltd v. Freehold Properties Ltd* (2002), Peter Gibson LJ said¹⁴⁸ (in a passage cited with approval by Lord Hoffmann in *Chartbrook Ltd v. Persimmon Homes Ltd*, 2009):¹⁴⁹

[I]t is necessary for the party seeking rectification and on whom the burden of proof lies, to demonstrate, on a balance of probabilities but by convincing proof, four matters: i) that the parties had a common continuing intention, whether or not amounting to an agreement, in respect of a particular matter in the instrument to be rectified; ii) that there was an outward expression of accord; iii) that the intention continued at the time of the execution of the instrument sought to be rectified; and iv) that by mistake the instrument did not reflect that common intention.

14.35 In greater detail, rectification requires satisfaction of these elements: (1) the court, exercising this equitable jurisdiction, can bring a written contract into conformity with the parties' pre-contractual and shared understanding of its terms if that understanding was 'outwardly manifested'; (2) identifying this understanding will involve objective interpretation of the parties' dealings, oral, written or in combination; (3) the Court of Appeal in *Joscelyne v. Nissen* (1970)¹⁵⁰ rejected the proposition that the prior accord must itself have been a specifically enforceable informal agreement; (4) the understanding must have continued unaltered until the time of formation (compare the *KPMG* case (2007), where the party seeking rectification failed to show such continuity;¹⁵¹ although the claimant succeeded in achieving a rewriting of the relevant clause using the technique of reconstitutive interpretation: see 14.21 ff); (5) the rectification doctrine is not confined to contracts but extends to 'instruments',¹⁵² a term of art which includes nominations of pensions beneficiaries¹⁵³ and rent notices.

The House of Lords in *Chartbrook Ltd v. Persimmon Homes Ltd* (2009)¹⁵⁴ confirmed these settled elements, notably propositions (1) to (3). In that case, in a *dictum* (too long to be reproduced here),¹⁵⁵ Lord Hoffmann explained how common intention, outwardly

¹⁴⁶ *Treitel* (12th edn, London, 2007), 8-064, cites cases concerning omission of customary terms.

¹⁴⁷ On estoppel by convention's overlap in this context, see *Mace v. Rutland House Textiles Ltd*, *The Times*, 11 January 2000 (Peter Leaver QC).

¹⁴⁸ [2002] 2 EGLR 71, at [33]; approved in *KPMG LLP v. Network Rail Infrastructure Ltd* [2007] EWCA Civ 363, at [17], by Mummery LJ.

¹⁴⁹ [2009] UKHL 38; [2009] 1 AC 1101, at [48].

¹⁵⁰ [1970] 2 QB 86, CA.

¹⁵¹ *KPMG LLP v. Network Rail Infrastructure Ltd* [2007] EWCA Civ 363, at [27], reversing the trial judge on this question of primary fact.

¹⁵² See note 135 above on the nature of 'instruments'.

¹⁵³ *Collins v. Jones*, *The Times*, 3 February 2000 (Stanley Burnton J).

¹⁵⁴ [2009] UKHL 38; [2009] 1 AC 1101, at [52] to [66].

¹⁵⁵ *Ibid.*, at [52] to [66].

manifested and objectively construed, might have supported rectification in that case (this point was a *dictum* because the House of Lords decided the case in favour of Persimmon on another ground, namely, on the basis of interpretation of the final text: for the facts of that case, see 14.23).

- 14.36** *Settled formula decisive.* When, during their negotiations, the parties have adopted a particular outward accord but the final document fails to reflect that earlier formulation, rectification will be available, but only to the extent of mirroring the verbal accord. The Court of Appeal in *Rose v. Pim* (1953) decided that rectification cannot be used to go behind that formulation and to unpick the parties' underlying confusion or ignorance concerning their transaction's subject matter or purpose.¹⁵⁶

In this case, the buyer received an order from a customer for 'Moroccan horsebeans known here as feveroles'. The seller innocently assured the buyer that 'horsebeans' and 'feveroles' were interchangeable words to describe the same type of bean. In fact, 'horsebean' is a generic term embracing feves, fevettes and feveroles. The parties settled upon the label 'horsebeans'. The agreement recorded accurately the parties' prior understanding that their contract was for 'horsebeans'. The buyer's customer really wanted 'feveroles'. But the buyer was instead supplied with feves, an inferior bean, or at least one not to the liking of the buyer's customer. The buyer was forced to sell the unwanted feves to a third party. The buyer sought rectification of the written contract to substitute 'feveroles' for 'horsebeans', which would then entitle the buyer to obtain damages for non-performance.

The Court of Appeal refused rectification: the written terms accurately reflected the outward accord (the word 'horsebeans'). As Morris LJ put it, this was a contract for 'horsebeans simpliciter' and not for 'horsebeans of the type feveroles'. The remedy of rescission was not available to the buyer because he had sold the unwanted consignment of 'feves' to a third party.

Denning LJ considered that the plaintiff had thrown away their best plea by abandoning at trial a claim for damages based on breach of a collateral warranty (9.05 to 9.10), namely, the contention that the seller had orally warranted that 'feveroles' were equivalent to 'horsebeans'. Treitel notes that the purchaser in this case might now have a remedy for damages under section 2(1) of the Misrepresentation Act 1967 (9.14) if he can show that the seller had had no reasonable grounds for believing the accuracy of its pre-contractual statement.¹⁵⁷

- 14.37** *Settled understanding but botched formula.* Arden J's decision in *Grand Metropolitan plc v. William Hill Group* (1997)¹⁵⁸ qualifies the principle, just explained, in *Rose v. Pim* (1953)¹⁵⁹ (14.36). Rectification can be granted if the following steps can be discerned: the

¹⁵⁶ [1953] 2 QB 450, CA; M. Smith, (2007) 123 LQR 116, 120–1.

¹⁵⁷ *Treitel* (12th edn, London, 2007), 8-066 n. 373.

¹⁵⁸ [1997] 1 BCLC 390, 394–5, 420.

¹⁵⁹ [1953] 2 QB 450, CA.

parties have enjoyed a clear understanding of the relevant matter or issue during their negotiations and there is objective evidence of that common understanding (unlike on the facts of *Rose v. Pim* where they were ‘all at sea’ on the relevant subject matter); the parties have then attempted to formulate this; but their chosen language fails to capture their true understanding; this clumsy formulation has been inserted into the final agreement.¹⁶⁰ According to Arden J, substance can prevail over form because the formula used fails to give proper effect to the underlying and clear consensus at which they were verbally aiming.

In *Grand Metropolitan plc v. William Hill Group* (1997),¹⁶¹ the contract did not reflect the parties’ common intention concerning the basis upon which the relevant company’s accounts would be drawn up. Arden J was able to identify such a common intention. However, the parties’ pre-contractual attempt to clothe that intention in words had been misconceived. The unfortunate wording was carried forward into the eventual written agreement. The judge held that equity could give effect to the underlying shared intention. This was not a case where the parties had settled upon an inappropriate label without understanding what the true purpose or underlying basis of their transaction was or might be.

It is submitted that Arden J’s decision in *Grand Metropolitan plc v. William Hill Group* (1997)¹⁶² is sound and that there is a true ground of distinction between that case and *Rose v. Pim* (1953).¹⁶³ This is also consistent with the following passage from Lord Hoffmann’s judgment in the *Chartbrook* case (2009),¹⁶⁴ which suggests that rectification can penetrate agreed but inapt formulae and give effect to clearly evidenced outward agreement concerning the relevant aspect of the transaction:

[I]t is generally accepted that Brightman J was right in *Re Butlin* [1976] Ch 251 in holding that rectification is available not only when the parties intended to use different words but also when they mistakenly thought their words bore a different meaning.

The horsebean case (*Rose v. Pim*)¹⁶⁵ (14.36) and company accounting basis cases (the *Grand Metropolitan plc* case;¹⁶⁶ see above) might be contrasted as follows. Suppose X and Y, who are ignorant of the language of board games and the niceties of chess and draughts, agree to play ‘a board game with black and white pieces’. Y is disappointed when X, in purported compliance with this agreement, wants to play draughts rather than chess because Y has since discovered that the latter is intellectually more challenging. Y cannot obtain an order to rectify this agreement to substitute ‘chess’ for the wording in

160 See Glanville Williams’ subtle comment, (1954) 17 MLR 154–5, cited by D. McLaughlan, (2008) 124 LQR 608, 615 n. 29.

161 [1997] 1 BCLC 390.

162 *Ibid.*

163 [1953] 2 QB 450, CA.

164 [2009] UKHL 38; [2009] 1 AC 1101, at [46].

165 [1953] 2 QB 450, CA.

166 [1997] 1 BCLC 390.

fact adopted. The parties were all at sea: they did not have a clue what they intended to agree upon. Contrast the situation where other parties have a shared and more concrete understanding of what they want to play: they want to play chess (which they have just witnessed being played), although they do not know the name for that particular game. Instead, they orally agree to play 'draughts'. This misnomer is inserted into their written contract. Rectification is possible because the agreed label 'draughts' can be shown to be inconsistent with an unaltered common intention to play chess (the game they both in fact aspired to play).

- 14.38 *Exclusionary bar on extrinsic evidence and parol evidence rule inapplicable.* When seeking to support a claim for rectification, a party is not prevented from adducing extrinsic oral or written evidence to determine the parties' pre-contractual intentions and negotiations. Nor, it seems, does an 'entire agreement' clause (9.27) preclude such an extrinsic search in order to consider the merits of a claim for rectification.¹⁶⁷ (On the exclusionary bar on evidence concerning pre-contractual negotiations, see 14.13 ff; on the parol evidence rule, see 14.26.)
- 14.39 *High standard of proof.* The party seeking rectification must satisfy a high standard of proof, especially where both parties have been professionally advised. Lawrence Collins J said in the *James Hay* case (2005): 'The burden is a particularly onerous one where there have been prolonged negotiations between the parties eventually assuming the shape of a formal instrument in which they have been advised by their respective legal advisers.'¹⁶⁸ He added:¹⁶⁹ 'Where experienced negotiators have reduced the agreement into a detailed, lengthy document, the task of showing that this document did not represent the parties' intention is "formidable"'
- 14.40 *Error of law.* Rectification should be available where the relevant drafting error arises from an error of law.¹⁷⁰ This argument is based on these analogous developments: the Court of Appeal in *Brennan v. Bolt Burdon* (2004) has confirmed that common mistake concerning a pure point of law can vitiate a contract (10.09);¹⁷¹ the fact/law distinction has been discarded by the House of Lords with respect to recovery of mistaken payments in *Kleinwort Benson Ltd v. Lincoln City Council* (1999);¹⁷² and the same distinction has been discarded in the law of misrepresentation (9.02).

167 *Chitty on Contracts* (30th edn, London, 2008), 5-112, citing *JJ Huber (Investments) v. Private DIY Co. Ltd* [1995] NPC 102.

168 *James Hay Pension Trustees Ltd v. Hird* [2005] EWHC 1093 (Ch), at [81], citing *Crane v. Hegeman-Harris Co. Inc.* [1939] 1 All ER 662, 664-5, Simonds J, affirmed [1939] 4 All ER 68, CA.

169 *James Hay Pension Trustees Ltd v. Hird* [2005] EWHC 1093 (Ch), at [81], citing *Snamprogetti International SA v. Phillips Petroleum* [2001] EWCA Civ 889, at [36].

170 Case law antedating these developments is collected at *Meagher, Gummow and Lehane's Equity: Doctrines and Remedies* (4th edn, Sydney, 2003), 26-060; R. Goff and G. H. Jones, *The Law of Restitution* (7th edn, London, 2007), 9.060.

171 [2004] EWCA Civ 1017; [2005] QB 303; this development is approved by Arden LJ in *Meretz Investments NV v. ACP Ltd* [2007] EWCA Civ 1303; [2008] Ch 244, at [118].

172 [1999] 2 AC 349, HL.

- 14.41 *Formal transactions.* Rectification can be granted to establish a written valid contract where the parties had clearly shared the intention that a contract for the conveyance of land would be effective.¹⁷³ Here, the remedy is effective to constitute an agreement which would otherwise be invalid for failure to satisfy formalities. A variation on this is a more recent English decision, where rectification was granted to revise a guarantee (the document had been signed by the guarantor, but its terms had not been properly recorded).¹⁷⁴
- 14.42 *Unilateral error not normally enough.* The starting point (see the next paragraph for qualifications) is the settled proposition, confirmed by the Court of Appeal in *Riverlate Properties Ltd v. Paul* (1975),¹⁷⁵ that a party cannot obtain rectification if he alone was mistaken concerning the terms of the final document.
- 14.43 *Rectification for an 'operative' unilateral error.* As Burrows observes, the relevant 'unilateral error' might concern a point of confusion which arose in one party's mind before, and independently of, the settling of the final written terms in binding contractual form.¹⁷⁶ But the more usual situation is a last minute problem: in reducing the terms into a final draft for the parties to clothe as their agreement, one of the parties, A, erroneously omits or adds, or 'botches', one or more of the terms; B is alive to this error, but he fails to point it out to A. It will be usual for the error to be detrimental to A, and correspondingly beneficial to B. But it seems that detriment to A is enough. Although the usual situation is that A's unilateral error is *known to B*, the jurisdiction to provide rectification is not confined to that situation. Thus, rectification can be awarded in favour of a mistaken party and against the non-mistaken party if:
- (1) A was not just in error but was the victim of B's undue influence;¹⁷⁷ or
 - (2) the error was fraudulently induced by B (authority for (1) and (2) is supplied by Slade LJ's statement in *Agip SpA v. Navigazione Alta Italia SpA* ('*The Nai Genova*') (1984),¹⁷⁸ where he said that 'estoppel, fraud, undue influence or breach of a fiduciary¹⁷⁹ relationship' might support a claim for rectification); or
 - (3) B, although 'aware' (whether actually aware, or effectively so: see 14.45) of A's error, unconscionably failed to draw to A's attention the fact that A was mistaken

173 *Domb v. Isoz* [1980] 1 Ch 548, 559, CA, *per* Buckley LJ (followed in *Sindel v. Georgiou* (1984) 154 CLR 661, 667–8; 55 ALR 1, 4–5, High Court of Australia).

174 *GMAC Commercial Credit Development Ltd v. Sandhu* [2004] EWHC 716 (Comm), Richard Siberry QC, at [50] to [58].

175 [1975] Ch 133, 141–5, CA.

176 Analysis of *A Roberts & Co. Ltd v. Leicestershire County Council* [1961] Ch 555, 570, Pennycuik J (on which see R. E. Megarry, (1961) 77 LQR 313–16 and A. Burrows, in A. Burrows and E. Peel (eds.), *Contract Terms* (Oxford, 2007), 88 ff).

177 *Snell's Principles of Equity* (31st edn, London, 2005), 14.15 nn. 86–8; *Spry's Equitable Remedies* (6th edn, Sydney, 2001), 608.

178 [1984] 1 Lloyd's Rep 353, 365, CA (cited in *Commission for New Towns v. Cooper (GB) Ltd* [1995] Ch 259, 279–80, CA).

179 *Calvert v. William Hill Credit Ltd* [2008] EWCA Civ 1427; [2009] Ch 330, at [53]; *Parker and Mellows: The Modern Law of Trusts* (9th edn, London, 2008), 10–048 ff; J. Edelman, 'When Do Fiduciary Duties Arise?' (2010) 126 LQR 302.

concerning the contents of the proposed final document;¹⁸⁰ in *Thomas Bates Ltd v. Wyndham's (Lingerie) Ltd* (1981), Buckley LJ said that this need not involve 'sharp practice' in a reprehensible sense.¹⁸¹

- 14.44 The sanction imposed by equity is that party B's failure to disabuse A of his error renders B subject to a contractual term or set of terms to which he did not positively agree. The objective principle of agreement requires that the party seeking rectification should bear a strong onus to substantiate these various allegations of impropriety. Some object that this involves equity imposing on the parties a version of a contract which does not reflect the parties' shared view or consensus. But (as noted by Briggs J in the *Chartbrook* case (2008) and quoted in part at 14.46) equity's intervention reflects the fact that B has elected to remain silent and so has not saved A from falling into the trap of assenting to written terms unacceptable to A (even though the trap was not necessarily 'set' by B, but was one which A happened to fall into, to B's knowledge).
- 14.45 For this purpose, B will be 'aware' of the other's error in any of three situations: (1) if he had actual knowledge, or (2) if he was wilfully blind to an obvious fact; or (3) if he wilfully or recklessly failed, contrary to the notion of reasonableness and honesty, to inquire whether there had in fact been a mistake.¹⁸² Of these three forms, (1) does not require proof of 'sharp practice';¹⁸³ but (2) or (3) requires a 'lack of probity' on B's part, perhaps even 'dishonesty'. (For the controversial judicial suggestion that this approach should extend to the situation where B has made no fraudulent misrepresentation, nor was B clearly aware of A's error, see the discussion of the *dictum* in the *Commission for New Towns* case at 14.48.) In *George Wimpey UK Ltd v. VI Components Ltd* (2005), both (i) the requirement of error on A's part and (ii) some form of knowledge on B's part were absent. As for (i), the Court of Appeal held that there was no evidence that A's board of directors (the 'decision-making' entity) had made an error.¹⁸⁴ As for (ii), even if, contrary to (i), A had been mistaken, it had not been shown that B, a relatively inexperienced party, knew of any such error. Therefore, B had not taken unfair advantage of A.
- 14.46 *Chartbrook Ltd v. Persimmon Homes Ltd* (2008) is another case illustrating the uphill task in proving that A suffered the requisite error and that B knew of it.¹⁸⁵ At first instance (on
- 180 *A Roberts & Co. Ltd v. Leicestershire County Council* [1961] Ch 555, 570, Pennycuik J (noted by R. E. Megarry, (1961) 77 LQR 313–16); '*The Olympic Pride*' [1980] 2 Lloyd's Rep 67, Mustill J; *Thomas Bates Ltd v. Wyndham's (Lingerie) Ltd* [1981] 1 WLR 505, CA; *Agip SpA v. Navigazione Alta Italia SpA* ('*The Nai Genova and the Nai Superba*') [1984] 1 Lloyd's Rep 353, 365, CA; *Commission for New Towns v. Cooper (GB) Ltd* [1995] Ch 259, CA (noted by D. Mossop, (1996) 10 *Journal of Contract Law* 259–63); *George Wimpey UK Ltd v. VI Components Ltd* [2005] EWCA Civ 77; [2005] 2 P & CR DG5; D. McLauchlan, 'The "Drastic" Remedy of Rectification for Unilateral Mistake' (2008) 124 LQR 608–40 (who thinks this category of rectification has been misunderstood: 14.47).
- 181 [1981] 1 WLR 505, 515, CA.
- 182 *Commission for New Towns v. Cooper (GB) Ltd* [1995] Ch 259, 281D, 292F, CA; *George Wimpey UK Ltd v. VI Construction Ltd* [2005] EWCA Civ 77; [2005] 2 P & CR DG5, at [79].
- 183 *Thomas Bates Ltd v. Wyndham's (Lingerie) Ltd* [1981] 1 WLR 505, 515H, CA, per Buckley LJ.
- 184 *George Wimpey UK Ltd v. VI Construction Ltd* [2005] EWCA Civ 77; [2005] 2 P & CR DG5.
- 185 [2008] EWCA Civ 183; [2008] 2 All ER (Comm) 387.

the House of Lords decision, which dispensed with the need to invoke rectification, see 14.23), Briggs J had said:¹⁸⁶

In unilateral mistake cases the reason why convincing proof is needed of the [defendant's] knowledge of the claimant's mistake is because of the inherent improbability that the [defendant] would behave so inequitably as to keep silent, once he knows about it.

The effect of a successful rectification claim based on unilateral mistake is always that it imposes a contract upon the defendant which he did not intend to make. It is the unconscionable conduct involved in staying silent when aware of the claimant's mistake that makes it just to impose a different contract upon him from that by which he intended to be bound. For that reason as well, convincing proof is needed that the defendant's conduct, taken as a whole, fell short of the requirements of good conscience.

14.47 McLaughlan has argued that the category of rectification for unilateral error known to the other party should be reconceptualised.¹⁸⁷ In his view, A is entitled to rectification in this context not because B has been aware of A's mistake and B's silence injects into the equation an inequitable or unconscionable factor. Instead, McLaughlan suggests that rectification gives effect to a *shared intention* in this context because A is 'led reasonably to believe that [B] assented to [A]'s understanding of the terms, so that rectification will give effect to the parties' agreement as objectively ascertained'.¹⁸⁸ This is an interesting suggestion, but two counter-remarks seem necessary. First, McLaughlan's notion can be explored by the English courts only at the highest level, because there is Court of Appeal authority that the test requires proof that B knew of A's error, or was wilfully blind, or wilfully or recklessly failed to inquire (14.43, 14.45). Secondly, McLaughlan's concept would involve a single criterion for rectification: the parties' pre-contractual dealings must reveal (i) a clearly articulated consensus ('common intention' rectification) or (ii) a set of terms to which B has positively or implicitly inclined (McLaughlan's reconstitution of the 'second head'). It is possible that limb (ii) might open the door too widely to disputes concerning rectification and so weaken the primacy of final written terms.

14.48 *Unilateral error and underhand negotiations.* In the *Commission for New Towns* case (1995), Stuart-Smith LJ¹⁸⁹ suggested that unilateral mistake can give rise to rectification if party B has deliberately lulled A into agreeing a document on terms which benefit B and harm A's interests. This involves B fraudulently creating a 'smokescreen' during negotiations. On this point, Stuart-Smith LJ's *dictum* reads:¹⁹⁰

186 *Chartbrook Ltd v. Persimmon Homes Ltd* [2007] EWHC 409 (Ch), *per* Briggs J, at [136].

187 D. McLaughlan, 'The "Drastic" Remedy of Rectification for Unilateral Mistake' (2008) 124 LQR 608, 610, 640.

188 *Ibid.*

189 *Commission for New Towns v. Cooper (GB) Ltd* [1995] Ch 259, 280, CA, this is a *dictum*.

190 [1995] Ch 259, 280, CA; expressly *dictum*. In Stuart-Smith LJ's original *dictum*, B was the mistaken party. In the quotation given here, A and B have been reversed in order to fit in with the rest of our discussion.

[W]ere it necessary to do so in this case, I would hold that where B intends A to be mistaken as to the construction of the [eventual] agreement, so conducts himself that he diverts A's attention from discovering the mistake by making false and misleading statements, and A in fact makes the very mistake that B intends, then notwithstanding that B does not actually know, but merely suspects, that A is mistaken and it cannot be shown that the mistake was induced by any misrepresentation, rectification may be granted.

Stuart-Smith LJ's suggestion, which is no more than a *dictum*, is that it will be unconscionable for B to take advantage of A's error even if A cannot clearly show that B did know of A's mistake at the time the contract was executed, and even if A cannot show that it was induced to agree as a result of a fraudulent misrepresentation by B.

The *Commission for New Towns* case concerned the following facts. The defendant tenant and plaintiff landlord had been engaged in negotiations relating to a subsisting lease. The court found that the tenant had conducted those negotiations in a manner calculated to cause the landlord to 'take its eye off the ball'. When these negotiations had concluded, the tenant contended that an express term of the new agreement gave him a right to surrender the lease to the landlord (a so-called 'put option'). The Court of Appeal's *ratio* in that case involved a simple point of construction: that the 'put option' was not part of the agreement. However, the court went on to suggest, by way of *dicta*, that, even if the document had contained such a provision, the landlord would have been entitled to rectify the document so as to delete this option. This would be justifiable because of the tenant's reprehensible bargaining strategy.

It is submitted that this suggested further route to rectification will carry little traffic because the main routes to 'non-consensual' rectification are fraudulent misrepresentation and acquiescence (14.43). Indeed, a future Court of Appeal should sceptically revisit Stuart-Smith LJ's *dicta*, and at the very least provide a clearer and more satisfactory rationale (the passage quoted above from Stuart-Smith LJ appears to be a curious hybrid of bad faith without proof of knowledge at the moment of contracting, and of misrepresentation without proof of inducement).

- 14.49 Third party rights.** Rectification will not be awarded if this would harm a third party who has, in good faith and for consideration, acquired rights in the relevant subject matter.¹⁹¹ But there must be good faith.¹⁹² Consider the case where the document which is to be rectified was between A and B, but the present dispute is between A and D. In this situation, rectification in favour of A, and to D's disadvantage, is available provided D is not a *bona fide* purchaser (as where it is shown that a portion of land was not intended to be included

191 *Smith v. Jones* [1954] 1 WLR 1089, 1091–3, *per* Upjohn J; *Snell's Principles of Equity* (31st edn, London, 2005), 14.19; *Chitty on Contracts* (30th edn, London, 2008), 5–130; *Meagher, Gummow and Lehane's Equity: Doctrines and Remedies* (4th edn, Sydney, 2003), 899 n. 31; A. Berg, (2008) 124 LQR 6, 12.

192 *Craddock Bros v. Hunt* [1923] 2 Ch 136, 151, 154–5, 158–9, CA, *per* Lord Sterndale MR and Warrington LJ (Younger LJ dissenting).

in the A/B transaction, and D knew that, following a blunder in the drafting of the A/B document, the literal terms of the A/D transaction purported to give D the same portion of land; rectification can be ordered of the A/B and A/D transactions; and D is in fact the trustee of the wrongly conveyed portion for the benefit of A, the original vendor).¹⁹³

- 14.50 *Acquiescence etc.* Rectification is barred by laches and acquiescence, although (according to most commentators) not by delay without more.¹⁹⁴ Affirmation, with knowledge of the right to rectification, is another bar.¹⁹⁵
- 14.51 *Arbitrator's power to order rectification.* An arbitration clause might be sufficiently widely drawn to permit an arbitrator to order rectification.¹⁹⁶ The Arbitration Act 1996 also permits an arbitrator to order rectification.¹⁹⁷

¹⁹³ *Ibid.*

¹⁹⁴ *Spry's Equitable Remedies* (6th edn, Sydney, 2001), 617–19; *Meagher, Gummow and Lehane's Equity: Doctrines and Remedies* (4th edn, Sydney, 2003), 899 and nn. 32 and 33; *Treitel* (12th edn, London, 2007), 8–072, appears to be alone in regarding 'lapse of time' as enough.

¹⁹⁵ *Butterworths Law of Contract* (3rd edn, London, 2007), 4.119; *Spry's Equitable Remedies* (6th edn, Sydney, 2001), 617–19.

¹⁹⁶ *Ashville Investments Ltd v. Elmer Contractors Ltd* [1989] QB 488, CA (wide review of the authorities).

¹⁹⁷ Section 48(5) of the Arbitration Act 1996.

Chapter contents

1. Introduction *para. 15.01*
2. Incorporation of exclusion clauses *para. 15.02*
3. Fraud and exclusion clauses *para. 15.04*
4. Strict interpretation at common law *para. 15.05*
5. Exclusion clauses and the Misrepresentation Act 1967 *para. 15.07*
6. Unfair Contract Terms Act 1977 *para. 15.08*
7. Unfair Terms in Consumer Contracts Regulations 1999 *para. 15.33*

15

Exclusion clauses

1. INTRODUCTION¹

15.01 Summary of main points

- (1) *Types of exclusion clause.* There are three main types of exclusion clause:
 - (a) total exclusion, 'X Co. will not be liable to you at all for breach of any of these obligations', sometimes known as an 'exemption clause';
 - (b) time restriction, 'If you want to claim compensation you must notify your claim within [a specified period] of the alleged harm';
 - (c) a financial cap, 'liability to pay compensation shall not exceed £X'.
- (2) *Common law responses to exclusion clauses.* This has been relatively feeble. The common law has tried to deal with the problem of exclusion clauses by employing three main techniques or rules: first, incorporation and 'notice'; secondly, 'construction' (that is, restrictive interpretation of written agreement *contra proferentem*, so as to lean against interpretation which might favour the person relying on the clause); thirdly, at common law, there is a rule invalidating attempts to exclude or restrict liability for fraud (15.04). Thus, before proceeding to consider the second stage of legal control, namely, statutory restrictions (on which see 15.08 and 15.33), at common law the three questions to be posed when considering an exclusion clause's effect are:
 - (a) Has the proposed exclusion clause become part of the contract (the question of 'incorporation' and of 'notice': 15.02 and 15.03)?
 - (b) If so, does the exclusion clause's wording cover the relevant head of loss (15.04 to 15.06)?
 - (c) Does the exclusion clause purport to exclude or restrict liability for fraud?²

¹ R. Lawson, *Exclusion Clauses and Unfair Contract Terms* (9th edn, London, 2008); *Chitty on Contracts* (30th edn, London, 2008), chapters 14 and 15; J. Cartwright, *Misrepresentation, Mistake and Non-Disclosure* (2nd edn, London, 2007), chapter 9; *Treitel* (12th edn, London, 2007), chapter 7.

² See previous note.

At common law, a clause can fail for *any* of the three reasons just mentioned at (a) to (c).

(3) *Issues arising under statute.* Here, the questions are:

- (a) Does the clause become automatically invalid under the statutory systems of control (notably, sections 2(1) and 6(1) and (2) of the Unfair Contract Terms Act 1977: see 15.13, 15.16, 15.17)?
- (b) Or, is the clause at least vulnerable to a statutory test of reasonableness, for example, under sections 2(1) or 3 of the Unfair Contract Terms Act 1977 (15.13 ff) or section 3 of the Misrepresentation Act 1967 (9.26) or the Unfair Terms in Consumer Contracts Regulations 1999 (15.33)? There are reasonableness tests contained in each of these statutory schemes.³

J. R. Spencer, 'Signature, Consent and the Rule in *L'Estrange v. Graucob*' [1973] CLJ 104

E. Peel, 'Whither *Contra Proferentem*?', in A. Burrows and E. Peel (eds.), *Contract Terms* (Oxford, 2007), chapter 4

E. MacDonald, 'Unfair Contract Terms Act – Thirty Years On', in A. Burrows and E. Peel (eds.), *Contract Terms* (Oxford, 2007), chapter 8

S. Bright, 'Unfairness and Consumer Contract Regulations', in A. Burrows and E. Peel (eds.), *Contract Terms* (Oxford, 2007), chapter 9

H. Beale, 'Exclusion and Limitation Clauses in Business Contracts: Transparency', in A. Burrows and E. Peel (eds.), *Contract Terms* (Oxford, 2007), chapter 10

H. Beale, 'Unfair Contract Terms in the Common Frame of Reference', in *Liber Amicorum Guido Alpa: National Private Law Systems* (London, 2007), 186

2. INCORPORATION OF EXCLUSION CLAUSES

15.02 *The test.* A line of common law decisions requires a party seeking protection from an exclusion clause to take reasonable steps to bring it to the other's attention. And so a clause becomes *incorporated* within the contract (although it might, at the next stage of inquiry, be invalidated as intrinsically unacceptable or 'unreasonable' in accordance with a statutory rule: see 15.08 ff) if either (1) the party purportedly subject to the exclusion clause knew that there was a contractual document containing terms or at

³ In 2005, this topic was declared to be under review by the English and Scottish Law Commissions: see Law Commission and the Scottish Law Commission, *Unfair Terms in Contracts* (Law Commission Report No. 292 and Scottish Law Commission Report No. 199, 2005), on which see H. Beale and T. Goriely, (2005) NLJ 318, 338; for earlier work by the Law Commissions, see Law Commission and the Scottish Law Commission, *Unfair Terms in Contracts* (Law Commission Consultation Paper No. 166 and Scottish Law Commission Discussion Paper No. 119, 2002), proposing a consolidated and coherent statute, and other changes.

least referring to them; or (2) the other party (now seeking to raise the exclusion clause as a defence) took reasonably sufficient steps to give the other side notice of the conditions. If so, the customer need not know that the relevant document consisted of, or referred to, contractual conditions; provided he was aware that the document contained writing.

There is case law support for this test. In *Parker v. South Eastern Railway Co.* (1877), a passenger had deposited a bag with contents exceeding the value of £10, but the receipt stated that it was a condition that the defendant company would not be liable for loss exceeding £10. The bag was lost. The Court of Appeal held that it would be enough that the passenger knew there was writing on the receipt, provided, it seems, that the relevant exclusion was not out of the ordinary. In this sense, the question was whether the defendant had taken adequate steps to bring home to such a customer of its services the relevant exclusion clause. Mellish LJ formulated this series of tests:⁴

[I]f the person receiving the ticket did not see or know that there was any writing on the ticket, he is not bound by the conditions; that if he knew there was writing, and knew or believed that the writing contained conditions, then he is bound by the conditions; that if he knew there was writing on the ticket, but did not know or believe that the writing contained conditions, nevertheless he would be bound, if the delivering of the ticket to him in such a manner that he could see there was writing upon it, was, in the opinion of the jury, reasonable notice that the writing contained conditions.

As noted by Megaw LJ in *Thornton v. Shoe Lane Parking* (1971):⁵

The essence of the decision in *Parker v. South Eastern Railway Co.* was analysed by Lord Hodson in *McCutcheon v. David MacBrayne Ltd* [1964] 1 WLR 125, 129, HL, as follows: ‘That case, affirmed in *Hood v. Anchor Line (Henderson Bros) Ltd* [1918] AC 837 established that the appropriate questions ... in a ticket case were: (1) Did the passenger know that there was printing on the railway ticket? (2) Did he know that the ticket contained or referred to conditions? and (3) Did the railway company do what was reasonable in the way of notifying prospective passengers of the existence of conditions and where their terms might be considered?’

Over a century later, Bingham LJ in *Interfoto v. Stiletto* (1989)⁶ noted that this ‘reasonable steps’ test applies not just to exclusion clauses but to all ‘onerous or unusual’ clauses lurking in the undergrowth of the other party’s standard terms (the clause in question in the *Interfoto* case concerned a special payment in the event of delayed return of hired material: see the text below).

⁴ (1877) 2 CPD 416, 423, CA.

⁵ [1971] 2 QB 163, 171–2, CA.

⁶ [1989] QB 433, CA; noted by H. McLean, [1988] CLJ 172; P. A. Chandler and J. A. Holland, (1988) 104 LQR 359; Sir Bernard Rix, ‘Lord Bingham’s Contributions to Commercial Law’, in M. Andenas and D. Fairgrieve (eds.), *Tom Bingham and the Transformation of the Law: A Liber Amicorum* (Oxford, 2009), 668–71.

In *Interfoto v. Stiletto* (1989),⁷ a commercial party, Stiletto, had hired transparencies from Interfoto, a photographic library. Stiletto was later invoiced for an exorbitant sum. Stiletto disputed liability to pay this amount. Interfoto's small-print terms imposed a large daily fee for each transparency if they were retained for longer than fourteen days, namely, £5 for each item for each extra day (it was thus a liquidated damages clause (19.01 ff) which smacked of a penalty). Interfoto's charges were about ten times higher than those charged by competitors. The eventual bill for late return was a massive amount, £4,000. The initial delivery note had been headed 'Conditions'. However, nothing more had been done to impress upon the customer the importance of these proposed terms. Nor had Stiletto signed to acknowledge notice of these terms. Although this term was not an exclusion clause, the Court of Appeal held that the nineteenth-century 'ticket' case law (concerning exclusion clauses) in fact applies to all 'onerous or unusual' clauses and not just exclusion clauses. The adequate notice test stated in the *Parker* case (1877) (see above) was not satisfied in the *Interfoto* case because the Court of Appeal held that Interfoto had not done enough to alert its customer to the especially onerous nature of the clause. And so the £4,000 contract claim failed.

For a case where the adequate notice test was satisfied, and where in any event the clause was neither 'onerous' nor 'unusual', see *O'Brien v. MGN Ltd* (2001).⁸ The *Interfoto* case overlaps with the (non-binding) UNIDROIT *Principles of International Commercial Contracts* (2004), Article 2.1.20,⁹ which refers to a 'term contained in standard terms which is of such a character that the other party could not reasonably have expected it', and requires such a clause to be 'expressly accepted' by the other party. However, as noted, the *Interfoto* case is not confined to 'standard terms' and the concept, adopted in that case, of 'onerous or unusual' clauses is wider than the approach employed in the 'soft law' codes, which refer to 'surprising terms'. Gloster J in *JP Morgan Chase Bank v. Springwell Navigation Corp.* (2008)¹⁰ noted various judicial discussions of the *Interfoto* decision.

15.03 There is extensive case law on other aspects of the issue whether an exclusion clause has been successfully incorporated into a contract. These matters can be categorised as follows.

- (1) A signature is effective to incorporate an exclusion clause. The common law rule is straightforward: if the innocent party has signed a document, he is taken objectively

⁷ *Ibid.*

⁸ [2001] EWCA Civ 1279; *The Times*, 8 August 2001; [2002] CLC 33; noted by J. Elvin, [2002] CLJ 19 ('scratch-card' winner; printed rules restricting winners to two in one week; neither 'onerous' nor 'unusual', *ibid.*, at [21] and [24]); similarly, *Photolibrary Group Ltd v. Burda Senator Verlag GmbH* [2008] EWHC 1343 (QB); [2008] 2 All ER (Comm) 881, at [12] and [60], *per* Jack J.

⁹ 2nd edn, Rome, 2004; see M. J. Bonell (ed.), *The UNIDROIT Principles in Practice: Case Law and Bibliography on the UNIDROIT Principles of International Commercial Contracts* (2nd edn, Ardsley, NY, 2006), 151 ff; S. Vogenauer and J. Kleinheisterkamp (eds.), *Commentary on the UNIDROIT Principles of International Commercial Contracts* (Oxford, 2009), 330 ff.

¹⁰ [2008] EWHC 1186, at [578] ff; affirmed [2010] EWCA Civ 1221.

to have assented to the exclusion clause, even if in fact he had not read it, or at least did not understand its effect. This was affirmed in *L'Estrange v. F Graucob Ltd* (1934), where the claimant had bought a defective cigarette slot machine for her Llandudno café.¹¹

In *L'Estrange v. F Graucob Ltd* (1934), Miss Harriett Mary L'Estrange, a café proprietor, bought an automatic slot machine (selling cigarettes) from the defendant company. The machine proved to be defective, soon becoming jammed and quite useless. But she had imprudently signed away nearly all her protection in a document containing small print. This included an exclusion clause: 'any express or implied condition, statement, or warranty, statutory or otherwise not stated herein is hereby excluded.' The Divisional Court held that her decision to sign this document and to conclude this agreement had the effect of incorporating the exclusion clause, whether or not she had in fact read or understood the clause. The court added that there are various exceptions to this, although none of these was satisfied on the present facts: duress; fraud; misrepresentation (see the *Curtis* case, summarised at 9.34); or the *non est factum* doctrine (10.20).¹² But none of these exceptions applied to the facts of this case.

The English decision in *L'Estrange v. Graucob* (1934) has been distinguished in Canada in *Tilden Rent-A-Car v. Clendenning* (1978), where it was held that signature is ineffective to incorporate a term if the *proferens* is aware that the signatory has not read an onerous clause, such as an exclusion clause (on the facts of the *Tilden* case, the relevant clause contained a strict limitation of the insurer's liability in a car-hire insurance policy).¹³ The Ontario Court of Appeal held that the defendant's signature on this contractual document was not decisive. The rental company obviously knew that the customer had not read the relevant clause in this document and that he was therefore unaware of this harsh and unusual term. For this reason, there was no justice in applying the blanket rule that signature incorporated all clauses, however surprising or unusual, and even if, to the other party's knowledge, the signatory had not bothered to read the document's relevant small print. This point is cogently made by John Spencer in his seminal treatment of this topic,¹⁴ and his argument was approved by the Ontario Court of Appeal in this case. The *Tilden* case's gloss upon the *L'Estrange* case seems sound: it is a modest additional requirement to require the signatory to sign, or at least to add his initials, to indicate assent to especially onerous clauses within such hire documents. Users of car hire will be familiar with this sensible practice.

11 [1934] 2 KB 394, Divisional Court; J. R. Spencer, 'Signature, Consent and the Rule in *L'Estrange v. Graucob*' [1973] CLJ 104.

12 *Gallie v. Lee* [1971] AC 1004, HL (for other cases, see 10.20).

13 (1978) 83 DLR (3d) 400; 18 OR (2d) 601.

14 J. R. Spencer, 'Signature, Consent and the Rule in *L'Estrange v. Graucob*' [1973] CLJ 103, 114–16.

- (2) Whether notification of the clause was too late because it occurred after the contract had already been formed. An exclusion clause will have no effect if it comes to a party's notice only after the contract has been formed.

In *Olley v. Marlborough Court Ltd* (1949), the claimant booked a room in a hotel.¹⁵ Later, some valuables were stolen from the room. The hotelier was guilty of negligence in allowing a thief access to the room. However, the defendant hotelier tried to escape liability for this negligence by relying on an exclusion clause placed in the hotel room. But this exclusion clause had not come to the claimant's notice until she had gone upstairs to her room. The court held that this clause had no effect because it had come to the claimant's notice too late.

Similarly, in *Thornton v. Shoe Lane Parking* (1971), the Court of Appeal held that notice of an exclusion clause came too late because the contract had already been formed once the driver of a car had entered the defendant's automated car park.¹⁶

- (3) Whether the clause was contained in a document which appeared to have contractual force.

In *Chapelton v. Barry Urban District Council* (1940), the claimant paid 2d (two old pence) for the hire of two deckchairs from the municipal authority (one for him, the other for his girlfriend, Miss Andrews). He fell through the canvas of one (not deliberately) and injured his back. He sued for breach of contract. The Court of Appeal held that the defendant's written exclusion clause – contained on the back of his receipt for the chairs – had not been incorporated. This document was not objectively intended to affect contractual rights. Slesser LJ said that the receipt was not a document which could reasonably be expected to contain terms. And MacKinnon LJ said that the defendant had not done enough to bring to the claimant's attention the condition on the back of the receipt.¹⁷

- (4) Whether the term had been incorporated by a consistent course of dealing between the parties.¹⁸ As for the 'battle of the forms' (on which 3.32 to 3.34), the Court of Appeal in *Tekdata Intercommunications v. Ampenol Ltd* (2009)¹⁹ acknowledged the authority of *Butler Machine Tool Co. Ltd v. Ex-Cell-O Corporation (England) Ltd* (1979), where the majority of the Court of Appeal (Lawton and Bridge LJ) adopted the 'last shot' approach.²⁰

- (5) Whether incorporation occurred on the basis of trade usage.²¹

¹⁵ [1949] 1 KB 532, CA.

¹⁶ [1971] 2 QB 163, CA.

¹⁷ [1940] 1 KB 532, CA.

¹⁸ *Chitty on Contracts* (30th edn, London, 2008), 12-011, citing extensive case law; see also *Photolibary Group Ltd v. Burda Senator Verlag GmbH* [2008] EWHC 1343 (QB); [2008] 2 All ER (Comm) 881.

¹⁹ [2009] EWCA Civ 1209; [2010] 1 Lloyd's Rep 357.

²⁰ [1979] 1 WLR 401, 405H, 406D, 407E, CA.

²¹ *British Crane Hire Corporation Ltd v. Ipswich Plant Hire Ltd* [1975] QB 303, CA; see 13.18.

3. FRAUD AND EXCLUSION CLAUSES

- 15.04 There is a common law principle invalidating as contrary to public policy attempts to exclude or restrict liability for fraud.²² The Court of Appeal in *Regus (UK) Ltd v. Epcot Solutions Ltd* (2008)²³ held that this common law bar encompasses ‘fraud or wilful, reckless or malicious damage’ but not an ordinary ‘intentional’ breach of contract (for the *presumption* that an exclusion clause does not cover deliberate breach, see 15.06).

4. STRICT INTERPRETATION AT COMMON LAW²⁴

- 15.05 The courts will adopt a strict interpretation of wide or unclear language contained in an exclusion clause (this is known as interpretation *contra proferentem*).²⁵ This restrictive style of interpretation works to the disadvantage of the so-called *proferens*, that is, the party seeking to put forward an exclusion clause (and some other analogous clauses). European consumer protection legislation, binding within England, extends this style of interpretation in favour of consumers who are subject to written terms contained in contracts for the supply of goods or services (15.39).²⁶ In particular, there is a common law rule that clear language must be used to exclude contractual liability for negligence. The House of Lords in the *HIH Casualty* case (2003) noted the continuing relevance of the so-called *Canada Steamships* case’s (1952) principles of construction.²⁷ These are:

- (1) Effect will be given to an *express exclusion of liability for negligence at common law* (although statute might nullify or modify this exclusion: see 15.13).²⁸
- (2) A clause will not be effective to exclude negligence if the relevant wording does not explicitly refer to negligence and if the language is wide enough to cover a ‘head of damage ... other than that of negligence ... which is not so fanciful or remote that the proferens cannot be supposed to have desired protection against it’.

22 *S Pearson & Son Ltd v. Dublin Corporation* [1907] AC 351, 353, 362, HL; considered in *HIH Casualty and General Insurance Ltd v. Chase Manhattan Bank* [2003] 2 Lloyd’s Rep 61, HL, at [16] *per* Lord Bingham, [98] *per* Lord Hobhouse (doubts, Lord Hoffmann at [76] and [81], and Lord Scott at [122]); noted by K. R. Handley, (2003) 119 LQR 537–41; *Granville Oils & Chemicals Ltd v. Davis Turner & Co. Ltd* [2003] EWCA Civ 570; [2003] 1 All ER (Comm) 819; [2003] 2 Lloyd’s Rep 356, at [13] ff.

23 [2008] EWCA Civ 361; [2009] 1 All ER (Comm) 586, at [33] ff.

24 E. Peel, ‘Whither Contra Proferentem?’, in A. Burrows and E. Peel (eds.), *Contract Terms* (Oxford, 2007), chapter 4. On the vitality of this approach, see the *William Hare* case [2010] EWCA 283, at [18].

25 R. Lawson, *Exclusion Clauses and Unfair Contract Terms* (9th edn, London, 2008); *Chitty on Contracts* (30th edn, London, 2008), chapter 14; J. Cartwright, *Misrepresentation, Mistake and Non-Disclosure* (2nd edn, London, 2007), chapter 9.

26 Regulation 7(2) of the Unfair Terms in Consumer Contracts Regulations 1999 (SI 1999 No. 2083) (15.39) contains a statutory version of the *contra proferentem* rule in favour of consumers.

27 *HIH Casualty and General Insurance Ltd v. Chase Manhattan Bank* [2003] 2 Lloyd’s Rep 61, HL, at [11], [59] to [63] and [95], citing *Canada Steamship Lines Ltd v. R* [1952] AC 192, 208, PC, *per* Lord Morton.

28 E.g. *outright prohibition*: sections 2(1) and 6(1) and (2) of the Unfair Contract Terms Act 1977 (see 15.13, 15.16 and 15.17 below), or it is at least vulnerable to a *statutory test of reasonableness*: e.g. sections 2(1) or 3 of the Unfair Contract Terms Act 1977 (see 15.13 ff below) or section 3 of the Misrepresentation Act 1967 (see 15.07 below) or the Unfair Terms in Consumer Contracts Regulations 1999 (SI 1999 No. 2083) (see 15.33 below): there are reasonableness tests contained in each of these statutory sets of provisions.

- 15.06 *Clear wording will be respected in exclusion clauses in a commercial context.* In *Photo Production Ltd v. Securicor Transport Ltd* (1980),²⁹ the House of Lords held that exclusion clauses can validly operate at common law, even if they concern major or core forms of breach, provided clear and unambiguous language is used. Lord Wilberforce said:³⁰

After [the Unfair Terms in Contract Terms Act 1977], in commercial matters generally when the parties are not of unequal bargaining power, and when risks are normally borne by insurance, not only is the case for judicial intervention undemonstrated, but there is everything to be said, and this seems to have been Parliament's intention, for leaving the parties free to apportion the risks as they think fit and for respecting their decisions.

And, in the same case, Lord Diplock said:³¹

In commercial contracts negotiated between businessmen capable of looking after their own interests and of deciding how risks inherent in the performance of various kinds of contract can be most economically borne (generally by insurance), it is ... wrong to place a strained construction upon words in an exclusion clause which are clear and susceptible of one meaning only even after due allowance has been made for the presumption [that the contract will contain the usual implied undertakings in the relevant context].

The House of Lords in the *Photo Production* case (1980) also rejected the so-called 'fundamental breach' doctrine. Lord Denning had been the main proponent of this doctrine, in the Court of Appeal in that case, and in several earlier cases. According to that now discredited view, exclusion clauses, even if clearly worded, could not validly exclude or restrict liability for serious breach of core contractual obligations. However, *Internet Broadcasting Corporation Ltd v. MAR LLC* (2009; also noted at 17.07)³² confirms that there is a presumption that an exclusion clause, although literally wide enough to cover this, will not be construed to protect a person (including a company controlled by an identifiable person) from liability for loss of profit flowing from a personal and deliberate repudiation of the relevant contractual undertaking.

5. EXCLUSION CLAUSES AND THE MISREPRESENTATION ACT 1967³³

- 15.07 This topic is examined in detail at 9.26. Here, it is enough to note that section 3 of the Misrepresentation Act 1967, applicable to all types of contract, authorises the court to invalidate a clause if it unreasonably excludes or restricts liability arising from a

29 [1980] AC 827, HL.

30 *Ibid.*, at 843.

31 *Ibid.*, at 850–1 (passage cited in *Deepak Fertilisers & Petrochemicals Corporation v. ICI Chemicals and Polymers Ltd* [1999] 1 Lloyd's Rep 387, CA, at [20]).

32 [2009] EWHC 844 (Ch); [2010] 1 All ER (Comm) 112; [2009] 2 Lloyd's Rep 295 (Gabriel Moss QC) (distillation of principles at [33]).

33 J. Cartwright, *Misrepresentation, Mistake and Non-Disclosure* (2nd edn, London, 2007), 9.18.

misrepresentation. The Court of Appeal in *Cremdean Properties Ltd v. Nash* (1977) said that, if the reality is that a misrepresentation was made, section 3 of the 1967 Act cannot be evaded by clauses which purport to deny that fact.³⁴

6. UNFAIR CONTRACT TERMS ACT 1977³⁵

- 15.08** *Scope of the Act.* In general, the controls upon exclusion clauses contained in the Unfair Contract Terms Act 1977 (UCTA) concern attempts to restrict or exclude liability arising in the course of the defendant's 'business' (see below).³⁶ (The exceptions, where the defendant need not be engaged in business, concern (1) title to goods, where UCTA's control applies whatever the status of the purchaser (15.16); and (2) statutory implied terms, where UCTA's control applies in favour of *consumer* purchasers (15.15).)

It is therefore often necessary to determine who is a 'consumer' for the purpose of UCTA (see the following comments). In essence, X will be a consumer if: (1) he is dealing with a party who is engaged in business; and (2) he is not acting in the course of business; (3) even if, with regard to *other transactions*, he (or that company or organisation) does engage in business; but (4) X cannot be a consumer if the dealing occurs at an auction or by competitive tender. These four points will now be glossed.

As for (1) and (2), a 'consumer' is defined by section 12(1)(a) and (b) of the Act: the consumer must 'neither [make] the contract in the course of business nor [hold] himself as doing so' and 'the other party [that is, the defendant] [must] make the contract in the course of business'.

As for (3), the Court of Appeal in *R & B Customs Brokers Ltd v. UDT Ltd* (1988) held that a company, which had purchased a car, had not dealt in the course of business and so had dealt 'as a consumer' because the transaction was not within the core of its business. The relevant transaction was the purchase of a car for the company's director: that company's normal business involved shipping agencies.³⁷

As for (4) someone buying at an auction or in a competitive tender is not a consumer: section 12(2) of UCTA.

- 15.09** UCTA contains a broad definition of exclusion clause which includes the following types of clause:³⁸

making the liability or its enforcement subject to restrictive or onerous conditions; excluding or restricting any right or remedy in respect of the liability or subjecting a person to any prejudice in consequence of his pursuing any such right or remedy; excluding or restricting rules of evidence or procedure.

³⁴ (1977) 244 EG 547, CA; E. Peel, (2001) 117 LQR 545, 549, also noting *South Western General Property Co. Ltd v. Marton* (1982) 263 EG 1090 and *St Marylebone Property Co. Ltd v. Payne* [1994] EGLR 25.

³⁵ E. MacDonald, 'Unfair Contract Terms Act – Thirty Years On', in A. Burrows and E. Peel (eds.), *Contract Terms* (Oxford, 2007), chapter 8.

³⁶ Section 14 of UCTA; this includes professional liability or the activities of a government department or a local or public authority.

³⁷ [1988] 1 WLR 321, CA.

³⁸ Section 13(1) of UCTA.

15.10 UCTA does *not* apply to all contracts: the *main* categories of exclusion (see Schedule 1 to the Act for full details) are:

- (1) insurance: Schedule 1 (excluding sections 2–4);
- (2) interests in land: Schedule 1 (excluding sections 2–4);
- (3) the creation or transfer of intellectual property rights: Schedule 1 (excluding sections 2–4);
- (4) the formation or dissolution of companies and the company's constitution: Schedule 1 (excluding sections 2–4);
- (5) securities: Schedule 1 (excluding sections 2–4);
- (6) contracts governed by international conventions: section 29;
- (7) contracts for international supply of goods: section 26 (and in *Trident Turboprop (Dublin) Ltd v. First Flight Couriers* (2009),³⁹ the Court of Appeal held that section 26 also disappplies section 3 of the Misrepresentation Act 1967: see 9.26);
- (8) contracts which would not be governed by English law if the parties had not expressly agreed to apply English law (contracts to which English law applies under a choice-of-law clause: see 12.05): section 27(1) (excluding sections 2–7).

15.11 *Three types of clause outside UCTA's definition of an exclusion clause.*

- (1) *Liquidated damages clauses.* The innocent party is entitled to the stipulated sum (provided it is not a penalty: 19.01 ff), even if that party's true loss is less than this sum. Such a clause can potentially benefit both parties because it might underestimate the actual loss suffered and so have an effect equivalent to a limitation clause (on such clauses, see 19.02 ff).
- (2) *After-the-event compromises or settlements.* Such an agreement, reached after the breach and loss, also falls outside UCTA's scope of exclusion clauses.⁴⁰
- (3) *Arbitration agreements.* UCTA excludes written commercial arbitration clauses (on which see 12.09) from its scope.⁴¹ But the Arbitration Act 1996 controls unfair arbitration clauses inserted to prevent an innocent consumer from litigating in the ordinary courts.⁴²

15.12 *Clauses defining the basic content of the obligation.* UCTA applies to clauses which narrow or exclude a party's substantive obligations in a way which runs counter to the innocent party's reasonable expectations in a particular context. Section 13(1) states:

39 [2009] EWCA Civ 290; [2010] QB 86, at [15] ff, *per* Moore-Bick LJ.

40 *Tudor Grange Holdings Ltd v. Citibank NA* [1992] Ch 53, 65–7, Browne-Wilkinson V-C.

41 Section 13(2) of UCTA.

42 Sections 89–91 of the Arbitration Act 1996; protection confined to claims not exceeding £5,000 (Unfair Arbitration Agreements (Specified Amount) Order 1999 (SI 1999 No. 2167); *Zealand v. Laing Homes Ltd* (2000) Technology and Construction LR 724, on which see *Chitty on Contracts* (30th edn, London, 2008), 14.128, 15.094, 32.013.

Sections 2 and 5 to 7 also prevent excluding or restricting liability by reference to terms and notices which exclude or restrict the relevant obligation or duty.

The courts apply this control by posing the question: In the absence of the clause in issue, would the other party have been entitled to performance of a duty on these facts? If the answer is 'yes', the clause is an exclusion clause; and so it will have no effect unless it satisfies the statutory reasonableness test (on that test, see 15.18 ff below).⁴³ Another provision applies the same approach. It controls contractual clauses purporting to entitle a party 'to render a contractual performance substantially different from that which was reasonably expected of him'.⁴⁴

15.13 Negligence. Sections 2(1) and (2) of UCTA control exclusion clauses intended to exclude or restrict liability for breach of a contractual obligation if that express or implied term requires the exercise of reasonable care.⁴⁵ Section 2(1) provides that an exclusion clause (or notice) cannot (in any circumstances) exclude or restrict liability for death or personal injury.⁴⁶ However, section 2(2) merely imposes a reasonableness test to determine whether to invalidate exclusion clauses concerning breach of a duty (contractual or tortious) to exercise reasonable care which results in loss *other than* personal injury or death, such as property damage or economic loss.

15.14 Standard written terms. Section 3 of UCTA is a broad provision. It is perhaps the most important control on exclusion clauses in the commercial sphere (especially for business-to-business relationships). Unlike section 2, section 3 can apply not only to exclusion clauses seeking to affect liability arising from breach of obligations to exercise reasonable care but also to liability for breach of *strict obligations* (although section 3 is not confined to strict obligations). Section 3 imposes a test of reasonableness (that test is examined below at 15.18). This provision covers two situations: (1) exclusion clauses between parties, *even if both are engaged in business*, where the clause is on the defendant's *standard written terms of business*;⁴⁷ and (2) exclusion clauses affecting *consumers even if such a clause is not contained in the defendant's standard written terms of business*. Of these, the first – the so-called 'business-to-business' facet of section 3 – is of great practical significance.⁴⁸ This facet of section 3 extends UCTA beyond *consumer* protection, so that it becomes a means of combating unjustified resort to exclusion clauses *as between businesses*. Here, the protective scheme of UCTA thus encroaches upon the hallowed principle of freedom of contract (1.08). That principle requires that businesses should

43 *Smith v. Eric S Bush Ltd* [1990] 1 AC 831, 857D, HL.

44 Section 3(20(b)) of UCTA.

45 Section 1(1) of UCTA; section 1(4) renders it immaterial whether the breach is inadvertent or intentional, or whether liability is personal or vicarious.

46 Section 14 of UCTA.

47 E.g. *St Alban's City and District Council v. International Computers Ltd* [1996] 4 All ER 481, 491, CA (terms 'standard' despite negotiations resulting in slight modification).

48 H. Beale, 'Exclusion and Limitation Clauses in Business Contracts: Transparency', in A. Burrows and E. Peel (eds.), *Contract Terms* (Oxford, 2007), chapter 10.

be accorded the power, without judicial interference, to write or agree their own terms of dealing, including terms restricting liability for contractual default. However, UCTA's protection might be justified as follows: there is a need, in extreme cases, to strike down exclusion clauses which very harshly tip the balance in favour of the defendant; this is especially important if the relevant exclusion is secreted in the defendant's standard terms of business; the other party might not have properly taken this exclusion clause into account. Section 3 recognises, therefore, that businesses (no less than consumers) might not be alert enough to spot and challenge exclusion clauses (for example, *Tekdata Intercommunications v. Ampenol Ltd* (2009),⁴⁹ examined at 3.32 to 3.34). Section 3 also reflects the fact that bargaining power between businesses is rarely equal, and sometimes the inequality can be severe. Finally, it should be recalled that the courts are not bound to invalidate such an exclusion clause. As the discussion below (15.18 to 15.30) shows, the courts exercise a statutory discretion when determining whether the clause is 'unreasonable', and hence invalid, taking into account a wide range of considerations. However, there is a counter-argument. The statutory 'reasonableness' test has the demerit of rendering uncertain the validity of standard form exclusion clauses in the business-to-business context contained within standard terms of business. In short, section 3, in so far as it permits business-to-business control of exclusion clauses in adhesion contracts, is a bold and debatable incursion by the British legislator into the commercial sphere.

- 15.15 *Statutory implied terms.* Such implied terms appear in contracts for the sale of goods, or for hire-purchase, or for the supply of goods and services.⁵⁰ In the case of implied terms inserted by statute into contracts for the sale of goods (or parallel terms inserted into hire-purchase agreements), UCTA applies whether or not the supplier was acting in the course of business.⁵¹
- 15.16 *Implied term concerning title to goods.* Liability arising from breach of the implied term that the seller (or party supplying goods under hire-purchase) has good title⁵² cannot be excluded or restricted, no matter what the status of the parties to the transaction is (that is, whether or not the innocent party is a consumer and whether or not the supplier is acting in the course of business).⁵³
- 15.17 *Other relevant statutory implied terms.* As for other relevant statutorily implied terms (as explained above), UCTA adopts a two-level system of control. If the innocent party is a 'consumer', the guilty party cannot exclude or restrict liability for breach of such an implied term.⁵⁴ If the innocent party is not a consumer, a party can exclude or restrict liability, but only 'in so far as the term satisfies the requirement of

49 [2009] EWCA Civ 1209; [2010] 1 Lloyd's Rep 357.

50 E.g. sections 13–15 of the Sale of Goods Act 1979.

51 Section 6(1) of UCTA.

52 E.g. section 12 of the Sale of Goods Act 1979.

53 Section 6(3) of UCTA.

54 Section 6(2) of UCTA.

reasonableness'.⁵⁵ Attempts wholly to exclude liability in commercial contracts for the supply of defective goods have been struck down as unreasonable.⁵⁶ This would be the likely outcome if the facts of *L'Estrange v. Graucob* (1934) were to recur (where the non-consumer purchaser was engaged in business: on this case, see 15.03 above).⁵⁷

15.18 *The test of 'reasonableness' under UCTA.* This Act confers wide-ranging discretionary powers on the courts to invalidate contractual exclusion clauses by reference to a test of reasonableness (see 15.19 below). The same criterion is used to control exclusion clauses falling within section 3 of the Misrepresentation Act 1967 (9.26).

15.19 Various provisions of UCTA require the courts to apply a test of 'reasonableness' to determine whether a particular clause is valid.⁵⁸ Guidelines assist the process of determining whether a clause is reasonable.⁵⁹ Section 11(2) of and Schedule 2 to UCTA provide five guidelines when determining whether the exclusion clause is reasonable. Those guidelines apply expressly to questions of reasonableness arising under sections 6 and 7 of UCTA, which concern the sale, hire-purchase and supply of goods. But the courts have extended the ambit of these guidelines by applying them to all questions of reasonableness within UCTA.⁶⁰ The guidelines in Schedule 2 to UCTA are as follows:

the strength of the bargaining positions of the parties relative to each other, taking account (among other things) alternative means by which the customer's requirements could have been met;

whether the customer received an inducement to agree to the term, or in accepting it had an opportunity of entering into a similar contract with other persons but without having to accept a similar term;

whether the customer knew or ought reasonably to have known of the existence and extent of the term (having regard, among other things, to any custom of the trade and any course of dealing between the parties);

where the term excludes or restricts any relevant liability if some condition is not complied with, whether it was reasonable at the time of the contract to expect that compliance with that condition would be practicable;

⁵⁵ Section 6(3) of UCTA.

⁵⁶ *Britvic Soft Drinks Ltd v. Messer Ltd* [2002] 1 Lloyd's Rep 20; [2002] 3 All ER (Comm) 321, CA (clause wholly excluding liability for failure to supply satisfactory goods was unreasonable); similarly, *Bacardi-Martini Beverages Ltd v. Thomas Hardy Packaging Ltd* [2002] EWCA Civ 549, CA.

⁵⁷ [1934] 2 KB 394, Divisional Court.

⁵⁸ Notably, sections 2(2), 3, 6(3) and 11 of, and Schedule 2 to, UCTA; for similar control, see section 3 of the Misrepresentation Act 1967 (9.26).

⁵⁹ Section 11(2) of UCTA; although confined to sections 6 and 7 of UCTA; the courts apply guidelines to parts of UCTA.

⁶⁰ *Chitty on Contracts* (30th edn, London, 2008), 14.092 to 14.099; *Schenkers Ltd v. Overland Shoes Ltd* [1998] 1 Lloyd's Rep 498, 505, CA; *Stewart Gill Ltd v. Horatio Myer & Co. Ltd* [1992] QB 600, 608, CA; *Monarch Airlines Ltd v. London Luton Airport Ltd* [1998] 1 Lloyd's Rep 403, 412, col. 1, Clarke J.

whether the goods were manufactured, processed or adapted to the special order of the customer.⁶¹

15.20 First instance decisions concerning the statutory test of reasonableness are not lightly to be upset on appeal: '[T]he appellate court should treat the original decision with the utmost respect and refrain from interference with it unless satisfied that it proceeded upon some erroneous principle or was plainly and obviously wrong.'⁶² There are many reported cases illustrating how the courts apply these provisions. UCTA places the burden of proof of satisfying the requirement of reasonableness on the party who seeks protection from the relevant clause.⁶³ This provision governs both the question of reasonableness under the 1967 Act (section 3, on which see 9.26) and under UCTA.⁶⁴

15.21 *Judicial overview of criteria.* Potter LJ in *Overseas Medical Supplies Ltd v. Orient Transport Services Ltd* (1999) summarised the factors relevant to this question of 'reasonableness':⁶⁵

the way in which the relevant conditions came into being and are used generally;

the five guidelines as to reasonableness set out in Schedule 2 [to UCTA];

[as for] equality of bargaining position the court will have regard not only to the question whether the customer was obliged to use the services of the supplier, but also the question how far it would have been practicable and convenient to go elsewhere;

the question of reasonableness must be assessed having regard to the relevant clause viewed as a whole; it is not right to take any particular part of the clause in isolation, although it must be viewed against a breach of contract which is the subject of the case;

the reality of the consent of the customer to the supplier's clause will be a significant consideration;

in cases of limitation rather than exclusion of liability, the size of the limit compared with other limits in widely used standard terms may also be relevant;

while the availability of insurance to the supplier is relevant, it is by no means a decisive factor;

61 E.g. *Edmund Murray v. BSP International Foundations Ltd* (1993) 33 Const LR 1, CA, discussed at 15.30 below.

62 *George Mitchell (Chesterhall) Ltd v. Finney Lock Seeds Ltd* [1983] 2 AC 803, 810, HL, per Lord Bridge.

63 Section 11(5) of UCTA.

64 Section 11(1) of UCTA, which refers compendiously to the 1967 and 1977 Acts.

65 [1999] 2 Lloyd's Rep 273, 276, CA.

the presence of a term allowing for an option to contract without the limitation clause but with a price increase in lieu is important; however, if the condition works in such a way as to leave little time to put such option into effect, this may effectively eliminate the option as a factor indicating reasonableness.

15.22 McKendrick has helpfully identified various factors (which can be summarised as follows):⁶⁶

- the meaning of the clause must first be ascertained;
- the greater the parties' equality of bargaining power, the more likely the clause will be regarded as reasonable (see 15.24);
- the clause must be tested at the moment of entry into the contract and not at the moment of breach;
- the court will consider the availability of insurance, but not the actual insurance position of the parties (see 15.26, 15.28);
- the court will also consider whether the clause has not in fact been consistently enforced by the defendant in its dealings with other customers (see 15.28);
- the court will note whether the clause deals with very different types of loss, so that a single limitation clause covers both types; if so, the clause might be inappropriate with respect to one of these heads (replicating the common law rules of interpretation: see 15.05 above);
- limitation clauses are more likely to pass the reasonableness test than total exclusion clauses, provided the limitation is realistic (see 15.25 and 15.27; but compare 15.28 and 15.29);
- the defendant should not pluck a figure out of the air; he should instead adopt some objective justification, such as its turnover, the insurance cover available, or the value of the contract.

Cases upholding clauses

15.23 *Defective software: supplier limiting liability to price paid: commercial customer.* In *Watford Electronics Ltd v. Sanderson CFL Ltd* (2001), the supplier of defective software to a commercial customer succeeded in restricting its liability for loss to the contract price.⁶⁷ A further exclusion of liability for indirect or consequential loss was also upheld as reasonable. Chadwick LJ gave weight to the following factors which tended to support a decision to uphold this exclusion clause:⁶⁸ (1) the significant risk that a non-standard or 'customised' software product might not perform satisfactorily; and the consequential risk that the commercial customer's operation might not be as profitable as it had expected; (2) the supplier is better placed to assess the risk of malfunction; but the customer is better

66 E. McKendrick, *Contract Law: Text, Cases and Materials* (4th edn, Oxford, 2010), 435 ff.

67 [2001] 1 All ER (Comm) 696; [2001] BLR 143, CA; noted by E. Peel, (2001) 117 LQR 545.

68 [2001] 1 All ER (Comm) 696; [2001] BLR 143, CA, at [54] to [56].

placed to assess the potential loss; (3) the risks were insurable (a factor given weight in the *Regus* case (2008));⁶⁹ (4) the parties had the opportunity, and indeed this was taken on the present facts,⁷⁰ to negotiate the price, taking into account these risks; and (5) experienced businessmen should be assumed to be the best judges of the commercial fairness of their agreements.

- 15.24 This last point is important. Chadwick LJ said that the courts should be ‘very cautious’ in invalidating as unreasonable (under the statute) an exclusion clause made between ‘experienced businessmen’ of equal bargaining strength unless ‘one party has, in effect, taken unfair advantage of the other or [the court is satisfied] that a term is so unreasonable that it cannot properly have been understood or considered.’ It is submitted that this approach is attractive (and Gloster J in *JP Morgan Chase Bank v. Springwell Navigation Corp.* (2008)⁷¹ has collected similar statements; and see also the *Regus* case (2008)).⁷² However, some puzzles remain. First, what is meant by ‘taking unfair advantage of the other’? Does this refer solely to misleading tactics during the negotiations? Secondly, when will a clause be ‘so unreasonable that it cannot properly have been understood or considered’? The statute refers to reasonableness, but the courts have substituted a notion of extreme unreasonableness. Is this acceptable?
- 15.25 *Limitation clauses or completely protective clauses in contracts between businesses.* Applying UCTA’s test of reasonableness, the courts have upheld *limitation* clauses: (1) imposing a restriction on an architect’s liability;⁷³ and (2) concerning liability for damage to other property (and associated loss) arising from the sale of bulk carbon dioxide.⁷⁴ However, clauses *wholly excluding* liability are less likely to be upheld as reasonable. Such a clause was in fact declared unreasonable in two cases concerning benzene traces in carbon dioxide supplied to manufacturers of soft drinks.⁷⁵
- 15.26 *Airport excluding liability to aircraft owner for negligence. Monarch Airlines Ltd v. London Luton Airport Ltd* (1998)⁷⁶ concerned damage to a commercial aircraft as a result of loose paving slabs on the defendant’s runway. The aircraft was insured for US\$30 million. Liability for simple negligence was excluded. The judge held that the exclusion clause was fair: the exclusion was generally accepted in this market, and insurance within the market was arranged on this basis.⁷⁷

69 *Regus (UK) Ltd v. Epcot Solutions Ltd* [2008] EWCA Civ 361; [2009] 1 All ER (Comm) 586, at [41] ff.

70 *Watford Electronics Ltd v. Sanderson CFL Ltd* [2001] 1 All ER (Comm) 696; [2001] BLR 143, CA, at [56].

71 [2008] EWHC 1186, Gloster J, at [603] ff; affirmed [2010] EWCA Civ 1221.

72 *Regus (UK) Ltd v. Epcot Solutions Ltd* [2008] EWCA Civ 361; [2009] 1 All ER (Comm) 586, at [40].

73 *Moore v. Yakely Associates Ltd* (1999) 62 Constr LR 76 (standard RIBA form, £250,000 limit).

74 *Britvic Soft Drinks Ltd v. Messer Ltd* [2002] 1 Lloyd’s Rep 20; [2002] 3 All ER (Comm) 321, CA: limitation clause point decided by Tomlinson J, not disturbed on appeal (and see next note).

75 *Britvic* case, *ibid.* (total exclusion clause for failure to supply satisfactory goods was unreasonable); similarly, *Bacardi-Martini Beverages Ltd v. Thomas Hardy Packaging Ltd* [2002] EWCA Civ 549, CA.

76 [1998] 1 Lloyd’s Rep 403.

77 *Ibid.*, at 414.

15.27 *Restriction upon consequential financial loss: defective software: restriction upheld.* In *Watford Electronics Ltd v. Sanderson CFL Ltd* (2001) (see also 15.23 on this case), the supplier of defective software to a commercial customer succeeded in capping its liability for loss by reference to the contract price.⁷⁸ A further exclusion of liability for indirect or consequential loss was also upheld as reasonable.

The meaning of 'consequential loss' in the context of exclusion clauses is disputed by McGregor, a leading commentator.⁷⁹ The Court of Appeal in *Hotel Services Ltd v. Hilton International etc. (UK) Ltd* (2002)⁸⁰ held that an exclusion clause which denies liability for 'consequential loss' should, in accordance with the *contra proferentem* style of interpretation (15.04), be construed as referring only to losses falling within the second part of the *Hadley v. Baxendale* remoteness rule (18.40). But McGregor has criticised this, suggesting that *Hadley v. Baxendale* remoteness is a red herring and that the *Hotel Services* case should be reconsidered by the Supreme Court in a future case. Instead, he suggests that 'consequential loss' should be held to cover all additional forms of loss, other than the failure to supply the promised subject matter.

Cases invalidating clauses

15.28 *Unreasonable limitation clause: commercial supply to farmer of defective seeds.* In *George Mitchell v. Finney Lock Seeds Ltd* (1983), the House of Lords invalidated a limitation clause in a sale between merchants.⁸¹ The case concerned defective cabbage seed supplied to the claimant, a farmer, by a seed-merchant, the defendant. The farmer had lost a 60-acre crop of cabbage, and his claim for lost revenue was over £60,000. But the limitation clause in the contract of sale limited liability to the purchase price, roughly £200. The House of Lords held that this clause was unreasonable and so invalid. In reaching this decision, the court considered these factors:

- it was usual in that business for a seed dealer to pay higher compensation as an *ex gratia* payment;
- this demonstrated that the defendant regarded the clause as unreasonable;⁸²
- seed merchants could obtain insurance without materially increasing their costs;
- the defendant should have realised that the variety of cabbage supplied by the defendant could not be grown commercially in the plaintiff's locality (East Lothian).

15.29 *Limitation clause: commercial supply of software to local authority.* In *St Albans City & District Council v. International Computers Ltd* (1996),⁸³ the defendant computer company,

78 [2001] 1 All ER (Comm) 696; [2001] BLR 143, CA; noted by E. Peel, (2001) 117 LQR 545.

79 *McGregor on Damages* (18th edn, London, 2009), 1-037 ff.

80 [2000] BLR 235, CA.

81 [1983] 2 AC 803, HL (decided pre-UCTA, but still useful for the articulation of factors).

82 A factor regarded by Lord Bridge as 'decisive' in [1983] 2 AC 803, HL (cf *Schenkers* case, [1998] 1 Lloyd's Rep 498, 508, CA, disregarding the fact that the clauses had not been rigorously applied during the parties' long-standing relationship).

83 [1995] FSR 686, 704–11, Scott Baker J, affirmed by the Court of Appeal, [1996] 4 All ER 481, noted by S. Hedley, [1997] CLJ 21 (but damages reduced because, in the following year, the local authority partially recouped this shortfall).

a big player in this market, supplied software to a local authority, and this would be used to enable the latter to compile a community charge (the poll tax) database. But the software contained an error. This caused the local authority to overestimate its population by 3 per cent. As a result, it did not recover as much money as it might have done. It claimed loss of over £1m (which the Court of Appeal later reduced). The computer company's exclusion clause limited liability to £100,000. The Court of Appeal upheld Scott Baker J's decision that this exclusion clause was invalid. The relevant factors (which were held to outweigh various competing factors: see the text below for these) were:⁸⁴

- the defendant company's economic size;
- the fact that the defendant had product liability insurance of £50m;
- there were few companies from which the plaintiff might have bought its software and all dealt on a standard basis;
- the authority's financial shortfall would otherwise be borne by the local population (reduced services or higher local taxes).

The competing factors, outweighed by the factors just recited, were:

- the general consideration that agreements should be given effect;
- the presumption that a contracting party agrees to the terms of a deal 'with his eyes open';
- the fact that such limitation of liability was standard in the software industry;
- software for sophisticated commercial or business use was a 'developing' area of technology.

In *Pegler Ltd v. Wang (UK) Ltd* (2000), another software case, Judge Bowsher QC declared unreasonable a clause which excluded liability for indirect, special and consequential loss (on this concept, see 15.27 above) and which imposed a two-year contractual limit for claims.⁸⁵ But this case seems to have turned on a special feature: that the supplier had made a misrepresentation concerning the equipment.

- 15.30** *Unreasonable restriction of liability: supplier of defective equipment attempting to confine liability to supply of replacement parts.* In *Edmund Murray v. BSP International Foundations Ltd* (1993), the claimant ordered a drilling rig from the defendant, who constructed it to the claimant's specification.⁸⁶ The rig was defective. The claimant sued for breach of contract. It was held that it was unreasonable for the defendant to exclude liability for breach of both express and implied terms for failure to satisfy these specifications and instead to restrict liability to the supply of spare parts. The court applied sections 3 and 7 of UCTA.

⁸⁴ Sections 3, 6 and 7 of UCTA.

⁸⁵ [2000] BLR 218.

⁸⁶ (1993) 33 Const LR 1, CA.

15.31 *Effect of statutory unreasonableness on offending clause.* The Court of Appeal in *Stewart Gill Ltd v. Horatio Myer & Co. Ltd* (1992)⁸⁷ held that, if part of an exclusion clause fails to satisfy the test of reasonableness, or is otherwise invalid under UCTA, the courts will not rewrite the clause in order to preserve any ‘reasonable’ part.⁸⁸

15.32 *Single clause containing separate sentences.* However, there is some scope for rescue. An apparently composite clause might be severable: if so, the severed part might then survive even though the other part is invalid.⁸⁹ In the *Watford Electronics* case (2001) (15.23), the Court of Appeal held that the following composite clause was severable, and that (contrary to the first instance judge’s decision) each sentence should be considered as a separate exclusion clause:

Clause 7.3 Neither the Company nor the Customer shall be liable for any claims for indirect or consequential losses [on this concept, see 15.27 above] whether arising from negligence or otherwise. In no event shall the Company’s liability under the Contract exceed the price paid by the Customer to the Company for the [software] connected with any claim.⁹⁰

However, practitioners should cautiously draft discrete exclusion clauses relating to different risks and liabilities. This will reduce the likelihood of one invalid provision causing another (otherwise valid) clause to fail.

7. UNFAIR TERMS IN CONSUMER CONTRACTS REGULATIONS 1999

15.33 *Summary.*

- (1) The Regulations cover many types of ‘unfair’ terms and not just exclusion clauses.
- (2) The protection is, however, confined to *consumers*, who must also be *natural persons* (as distinct from companies or public authorities).
- (3) The other party must be engaged in *business* as a supplier of goods or services.
- (4) Core terms, such as the price or remuneration and the ‘definition of the main subject matter’ of the transactions, are free from control under the Regulations (but even core terms must be couched in language which is ‘plain and intelligible’: see 15.39).
- (5) A non-core term will be unenforceable under the Regulations if: (a) the relevant term has not been individually negotiated; (b) the term operates contrary to ‘good

⁸⁷ [1992] QB 600, CA.

⁸⁸ *Stewart Gill Ltd v. Horatio Myer & Co. Ltd* [1992] QB 600, CA; and *Thomas Witter Ltd v. TBP Industries Ltd* [1996] 2 All ER 573, 597–8, Jacob J; generally see *Chitty on Contracts* (30th edn, London, 2008), 14.100 to 14.102.

⁸⁹ *Edmund Murray v. BSP International Foundations Ltd* (1993) 33 Const LR 1, CA (remitting the severance issue to the trial judge).

⁹⁰ This case was applied in *Regus (UK) Ltd v. Epcot Solutions Ltd* [2008] EWCA Civ 361; [2009] 1 All ER (Comm) 586, at [44] ff.

faith'; and (c) the term 'causes a significant imbalance in the parties' rights and obligations arising under the contract, to the detriment of the consumer'.

- (6) This set of rules (first enacted in 1994) is a creature of European Union law. The 1999 Regulations (their predecessor was the 1994 set of Regulations) implement a Council Directive.⁹¹
- (7) The Regulations operate in parallel to UCTA (see 15.08 ff). This creates a 'complicated dual system of protection'. In 2000, the Law Commission set about the difficult task of welding the two statutory regimes into a single set of provisions.⁹²

15.34 *Scope of Regulations.* The Regulations are in some respects narrower, but in other respects broader, than UCTA (see 15.08 ff). Thus, the Regulations: (1) only apply to contractual terms;⁹³ (2) are not restricted to exclusion clauses;⁹⁴ (iii) do not apply to terms which are 'individually negotiated';⁹⁵ and (iv) only apply where the seller or supplier acts for 'purposes relating to his trade, business or profession'⁹⁶ and the other party is a consumer, that is, a natural person 'acting for purposes which are outside his trade, business or profession'. Furthermore (5) the Regulations only apply to the supply of goods or services⁹⁷ (the Court of Appeal has applied the Regulations to the relations between landlord and tenant, where the tenant was a 'consumer' of services).⁹⁸

15.35 *Consumer protection only.* Although the seller or supplier can be an individual or a 'legal person' (that is, it might be a company),⁹⁹ the recipient of these goods or services must be a 'consumer'¹⁰⁰ who is a flesh-and-blood 'natural person'.¹⁰¹ In one case, a civil engineer and lawyer were held to be consumers for this purpose even though the relevant transactions concerned foreign exchange deals totalling US\$7m.¹⁰² The judge was satisfied that the deals were aimed at satisfying the parties' private needs, namely, appropriate use of their income.

91 Unfair Terms in Consumer Contracts Regulations 1999 (SI 1999 No. 2083); see also Unfair Terms in Consumer Contracts (Amendment) Regulations 2001 (SI 2001 No. 1186); *Chitty on Contracts* (30th edn, London, 2008), chapter 15; S. Bright, 'Unfairness and Consumer Contract Regulations', in A. Burrows and E. Peel (eds.), *Contract Terms* (Oxford, 2007), chapter 9; for discussion of the 1993 Directive, see 'Report on Directive 93/13/EEC on Unfair Terms in Consumer Contracts', COM (2000) 248 final, 27 April 2000; H. Beale, 'Unfair Contract Terms in the Common Frame of Reference', in *Liber Amicorum Guido Alpa: National Private Law Systems* (London, 2007), 186.

92 Law Commission and the Scottish Law Commission, *Unfair Terms in Contracts* (Law Commission Consultation Paper No. 166 and Scottish Law Commission Discussion Paper No. 119, 2002).

93 Section 2 of UCTA is wider and includes tortious negligence.

94 UCTA is predominantly concerned with exclusion clauses: sections 1–7.

95 Regulation 5(1) to (4) of the Unfair Terms in Consumer Contracts Regulations 1999 (SI 1999 No. 2083).

96 Regulation 3(1), *ibid.*

97 The key part (reg. 4(1)) of the 1999 Regulations does *not* refer to 'goods' or 'services', but, untidily, reg. 6(2)(b) does.

98 *UK Housing Alliance (North West) Ltd v. Francis* [2010] EWCA Civ 117; [2010] 3 All ER 519; see also *Office of Fair Trading v. Foxtons Ltd* [2009] EWCA Civ 288; [2010] 1 WLR 663.

99 Cf UCTA allows companies to be 'consumers': section 12 of UCTA.

100 Section 90 of the Arbitration Act 1996 extends the Regulations' reference to consumers to include legal persons as well as natural persons in the context of invalidating consumer arbitration clauses (under sections 89–91 of the 1996 Act).

101 Regulation 3(1) of the Unfair Terms in Consumer Contracts Regulations 1999 (SI 1999 No. 2083).

102 *Standard Bank London Ltd v. Apostolakis* [2000] ILPr 766, Commercial Court, Longmore J ('consumers' attacked exclusive jurisdiction clause).

15.36 *Limits on protection.* The Regulations do not disturb terms which define the ‘main subject matter of the contract’ or ‘the adequacy of the price or remuneration, as against the goods or services supplied in exchange’. Regulation 6(2) states:

In so far as it is in plain intelligible language, the assessment of fairness of a term shall not relate—

- (a) to the definition of the main subject matter of the contract, or
- (b) to the adequacy of the price or remuneration, as against the goods or services supplied in exchange.

In *Director General of Fair Trading v. First National Bank plc* (2002),¹⁰³ the House of Lords held that these ‘core’ elements of a transaction must be accorded a sensible and non-expansive interpretation, otherwise the overall protective function of those Regulations would be weakened (this case is further discussed at 15.38). Lord Steyn said that a ‘restrictive’ approach is required to prevent ‘endless formalistic arguments as to whether a provision is a definitional or an exclusionary provision’.¹⁰⁴ And Lord Bingham said:¹⁰⁵ ‘The object of the Regulations and the [1993] Directive is to protect consumers against the inclusion of unfair and prejudicial terms in standard-form contracts into which they enter, and that object would plainly be frustrated if Regulation 3(2)(b) were so broadly interpreted as to cover any terms other than those falling squarely within it.’

In *Office of Fair Trading v. Abbey National plc* (2009),¹⁰⁶ the Supreme Court (reversing the Court of Appeal)¹⁰⁷ held that bank charges for unauthorised overdrafts on current accounts constituted a ‘core’ matter. They concerned the ‘adequacy of the price or remuneration, as against the goods or services supplied in exchange’ (the exemption contained in Regulation 6(2)(b)). And so such bank charges cannot be attacked under these Regulations. Lord Phillips said:¹⁰⁸

Banks now rely on the Relevant Charges as an important part of the revenue that they generate from the current account services. If they did not receive the Relevant Charges they would not be able profitably to provide current account services to their customers in credit without making a charge to augment the value of the use of their funds.

Lord Mance said:¹⁰⁹

[T]here is no reason why the price or remuneration payable for a package of services should not consist of a contingent liability. The uneconomic nature of the Relevant

¹⁰³ [2002] 1 AC 481, HL; C. MacMillan, [2002] CLJ 22; *Chitty on Contracts* (30th edn, London, 2008), chapter 15.

¹⁰⁴ [2002] 1 AC 481, HL, at [34].

¹⁰⁵ *Ibid.*, at [12].

¹⁰⁶ [2009] UKSC 6; [2009] 3 WLR 1215 (noted by M. Chen-Wishart, (2010) 126 LQR 157).

¹⁰⁷ [2009] EWCA Civ 116; [2009] 2 WLR 1286 (noted by M. Chen-Wishart, (2009) 125 LQR 389–93).

¹⁰⁸ [2009] UKSC 6; [2009] 3 WLR 1215, at [88].

¹⁰⁹ *Ibid.*, at [117].

Charges from the customers' viewpoint constitutes the importance of the charges from the banks' viewpoint, and the plain intelligible language of the banking contracts made evident that there must be a considerable element of cross-subsidy in respect of customers while they remained in credit.

15.37 *Criteria of unfairness.* The core of protection under the 1999 Regulations comprises three elements. A term is not binding on the consumer¹¹⁰ if:

- (1) it is contrary to the requirement of 'good faith';¹¹¹ and
- (2) 'it causes a significant imbalance in the parties' rights and obligations arising under the contract, to the detriment of the consumer';¹¹² provided
- (3) the term has not been individually negotiated.¹¹³

The Regulations state that this last requirement is not satisfied if 'the consumer has ... not been able to influence the substance of the term',¹¹⁴ but the Court of Appeal has added that 'it does not follow from the existence of the ability to influence the substance of the term that the term has, in fact, been individually negotiated. That is still a matter for the supplier to prove.'¹¹⁵

The Regulations provide 'non-exhaustive' and 'indicative' examples of terms having the potential to infringe this regime of control¹¹⁶ (effectively, a 'grey list' of possible, or even probable, invalidity).

15.38 The House of Lords in *Director General of Fair Trading v. First National Bank plc* (2002)¹¹⁷ said that the requirement of 'good faith' involves, first, that the consumer should not be taken unfairly by surprise, and, secondly, that his 'reasonable expectations' should not be defeated.¹¹⁸ Lord Bingham said:¹¹⁹

The requirement of good faith in this context is one of fair and open dealing. Openness requires that the terms should be expressed fully, clearly and legibly, containing no concealed pitfalls or traps.

¹¹⁰ Regulation 8(1) of the Unfair Terms in Consumer Contracts Regulations 1999 (SI 1999 No. 2083).

¹¹¹ Considered in *UK Housing Alliance (North West) Ltd v. Francis* [2010] EWCA Civ 117; [2010] 3 All ER 519, at [29], where the consumer's challenge to the relevant term failed.

¹¹² Considered, *ibid.*, at [26] ff, where the consumer's challenge to the relevant term failed.

¹¹³ See reg. 5 of and Schedule 2 to the Unfair Terms in Consumer Contracts Regulations 1999 (SI 1999 No. 2083) for an 'indicative and non-exhaustive list of the terms which may be regarded as unfair' (the so-called 'grey list').

¹¹⁴ Regulation 5(2), *ibid.*

¹¹⁵ *UK Housing Alliance (North West) Ltd v. Francis* [2010] EWCA Civ 117; [2010] 3 All ER 519, at [19], *per* Longmore LJ.

¹¹⁶ Schedule 2 to the Unfair Terms in Consumer Contracts Regulations 1999 (SI 1999 No. 2083).

¹¹⁷ [2002] 1 AC 481, HL, noted by C. MacMillan, [2002] CLJ 22.

¹¹⁸ Citing H. Beale, in J. Beatson and D. Friedmann (eds.), *Good Faith and Fault in Contract Law* (Oxford, 1995), chapter 9, at 245; on 'good faith' in civilian systems, see R. Zimmermann and S. Whittaker (eds.), *Good Faith in European Contract Law* (Cambridge, 2000).

¹¹⁹ [2002] 1 AC 481, HL, at [17].

And:

Fair dealing requires that a supplier should not, whether deliberately or unconsciously, take advantage of the consumer's necessity, indigence, lack of experience, unfamiliarity with the subject matter of the contract, weak bargaining position or any other factor [in Schedule 2].¹²⁰

No violation was found on the facts of this case. This was a test case concerning a giant loan company. This company's standard terms provided that the debtor should continue to pay the contractual rate of interest even after a court had given judgment in favour of the creditor. Statutory rules provided that, after a judgment, the debt should become payable in instalments. But the statutory rates of interest were lower than those provided in the contract itself. The contract stated that these higher rates of interest would remain payable until the debt was fully discharged (and the statutory default rules were thus contractually excluded). The House of Lords held that this demanding contractual rate of interest could not be invalidated as being unfair under the Regulations (the House of Lords were applying the then applicable 1994 Regulations, but the 1999 version would not change the result). It was not a 'core' provision but an ancillary provision, and so the Regulations applied.¹²¹ However, the House of Lords refused to invalidate this clause, Lord Bingham concluding:¹²² 'On balance, I do not consider that the term can properly be said to cause a significant imbalance in the parties' rights and obligations under the contract to the detriment of the consumer in a manner or to an extent which is contrary to the requirement of good faith.'

- 15.39** *Clear language required.* Regulation 7 of the 1999 Regulations requires written terms to be expressed in 'plain, intelligible language'. Where there is doubt, this interpretation should be resolved in favour of the consumer. This is a free-standing aspect of the Regulations. The 'plain, intelligible language' requirement is thus capable of being invoked to challenge even 'core' provisions of the relevant contract.

This last point was made clear in *Bankers Insurance Co. Ltd v. South* (2003),¹²³ where the relevant clause provided: 'For each person insured we will NOT pay ... compensation or other costs arising from accidents involving your ownership or possession of any ... motorized waterborne craft.' South had hired a jet ski and had injured Gardner. The parties conceded that the clause just cited was a 'core' term under the Regulations (and it should be noted that UCTA does not apply at all to insurance contracts). And so the only possible basis of statutory challenge was that the clause failed the plain intelligible language criterion. Buckley J held that it did not fail that test.

¹²⁰ *Ibid.*

¹²¹ *Ibid.*, at [12], *per* Lord Bingham.

¹²² *Ibid.*, at [24].

¹²³ [2003] EWHC 380 (QB).

- 15.40 *Agreed penalties.* The Regulations presumptively invalidate a stipulation requiring a consumer to pay ‘a disproportionately high sum in compensation’, and this therefore overlaps with the common law’s penalty jurisdiction (19.02 ff).¹²⁴
- 15.41 *Enforcement proceedings.* Besides individual civil proceedings by a consumer, either as claimant or defendant, the Office of Fair Trading and other ‘qualifying bodies’¹²⁵ can bring civil actions to tame unfair clauses by obtaining injunctions.¹²⁶ Such injunctions can extend to ‘similar’ terms ‘used or recommended for use by any person’, that is, not just the defendant. In other words, such injunctions need not be limited to matters *inter partes* but can be used against persons generally. Mulheron has examined the procedural background to enforcement in this context.¹²⁷

124 Schedule 2(1)(e) to the Unfair Terms in Consumer Contracts Regulations 1999 (SI 1999 No. 2083).

125 See the bodies mentioned at *Chitty on Contracts* (30th edn, London, 2008), 14.131 (noting the Enterprise Act 2002, in the context of the Unfair Contract Terms Act 1977); and, on the 1999 Regulations, *ibid.*, at 15.137 and 15.138; S. Bright, (2000) LS 331, 333–8, 352.

126 Regulations 10, 11 and 12 of and Schedule 1 to the Unfair Terms in Consumer Contracts Regulations 1999 (SI 1999 No. 2083); applied in *Office of Fair Trading v. Foxtons Ltd* [2009] EWCA Civ 288; [2010] 1 WLR 663.

127 Chapter 10 in *Reform of Collective Redress in England and Wales*, www.civiljusticecouncil.gov.uk/files/collective_redress.pdf. As for compensatory damages on behalf of a represented class of ‘victims’, the government in July 2009 rejected the suggestion that there should be a generic opt-out reform: see *The Government’s Response to the Civil Justice Council’s Report Improving Access to Justice Through Collective Actions*, www.justice.gov.uk/government-response-cjc-collective-actions.pdf.

VII

Breakdown and liability

Chapter contents

1. Introduction *para.* 16.01
2. Main threads of the doctrine *para.* 16.02
3. The scope of frustration *para.* 16.07
4. Default and self-induced frustration *para.* 16.15
5. The aftermath of frustration *para.* 16.21
6. Termination of contracts of indefinite duration *para.* 16.30
7. Post-formation hardship: exceptional denial of specific performance *para.* 16.31

16

Frustration

1. INTRODUCTION¹

16.01 Summary of main points

- (1) Frustration is a narrow doctrine; it is not enough that a contract becomes unexpectedly difficult or more expensive to perform on one or both sides; the courts will not relieve a party from a merely onerous turn of events.² English judges possess no general power to absolve contracting parties from their obligations on the ground of hardship arising after formation.³ Aggravating circumstances, even a commercial crisis for the relevant party, will not constitute frustration⁴ unless Lord Radcliffe's test in *Davis Contractors Ltd v. Fareham Urban District Council* (1956)⁵ (cited at 16.02) can be satisfied.
- (2) The modern frustration doctrine concerns three situations: (a) supervening illegality, that is, performance of the contract becomes illegal because of a legal change subsequent to

1 G. H. Treitel, *Frustration and Force Majeure* (2nd edn, London, 2004); E. McKendrick (ed.), *Force Majeure and Frustration of Contract* (2nd edn, London, 1995); a comparative study is B. Nicholas (1974) 48 *Tulane Law Review* 946; for other approaches, see E. McKendrick, *Contract Law: Text, Cases and Materials* (4th edn, Oxford, 2010), 752–3, noting the Vienna Convention on Contracts for the International Sale of Goods, the *Principles of European Contract Law* and the UNIDROIT Principles; W. Lorenz, 'Contract Modification as a Result of Change of Circumstances', in J. Beatson and D. Friedmann (eds.), *Good Faith and Fault in Contract Law* (Oxford, 1995), 357.

2 *British Movietoneux Ltd v. London & District Cinemas Ltd* [1952] AC 166, 183–4, 188, HL, *per* Viscount Simon and Lord Simonds.

3 *British Movietoneux* case, [1952] AC 166, 185, HL (repudiating Denning LJ's unorthodox leniency in the lower court, at [1951] 1 KB 190, 201–2, CA); *cf* no repentance shown by Lord Denning MR in his minority judgment in *Staffordshire Area Health Authority v. South Staffordshire Waterworks Co.* [1978] 1 WLR 1387, 1397–8, CA: 17.04 and 16.30).

4 *Pioneer Shipping Ltd v. BTP Tioxide Ltd ('The Nema')* [1982] AC 724, 752, HL, *per* Lord Roskill; *J Lauritzen AS v. Wijsmuller BV ('The Super Servant Two')* [1990] 1 Lloyd's Rep 1, 8, CA, *per* Bingham LJ.

5 *Davis Contractors Ltd v. Fareham Urban District Council* [1956] AC 696, 729, HL, *per* Lord Radcliffe; considered in *Pioneer Shipping Ltd v. BTP Tioxide Ltd ('The Nema')* [1982] AC 724, 744, 751–2, HL, *per* Lords Diplock and Roskill; *'The Great Peace'* [2002] EWCA Civ 1407; [2003] QB 679, at [70].

the contract's formation;⁶ (b) other instances of impossibility; or (c) severe obstruction of contractual performance ('frustration of the venture'; sometimes referred to as 'frustration of the purpose' by some modern commentators), although this third category is very seldom successfully pleaded.

- (3) Frustration is concerned with drastic changes occurring after the contract's formation. The doctrine has the effect of terminating the contract by operation of law, that is, without either party needing actively to bring it to an end. As Lord Sumner said in the Privy Council in the *Hirji Mulji* case (1926), 'frustration brings the contract to an end forthwith, without more and automatically' (that is, without any need for the parties to be aware that it has occurred)⁷ (16.21). The effect of such termination is that the parties are released from their future obligations under the contract. As for the position after this termination, the Law Reform (Frustrated Contracts) Act 1943 has ameliorated the common law consequences of frustration: the effect of such termination is that the parties are released from their future obligations under the contract.
- (4) Frustration operates only if the contract contains neither an express⁸ nor an implied⁹ allocation of the relevant risk to one of the parties (for the parallel approach within the doctrine of mistake, see 16.03).
- (5) *Force majeure* clauses, or related provisions inserted by agreement into the relevant transaction, often declare when a party will be released from his obligations by reason of freak and excusable supervening events.¹⁰
- (6) If an event is foreseen or foreseeable, it is less likely that the doctrine of frustration will arise.
- (7) Various types of 'default' by a party will also preclude frustration. These situations are known collectively as 'self-induced frustration'. The party who has culpably induced frustration will normally be in breach of contract.

6 Section 1(1) of the Law Reform (Frustrated Contracts) Act 1943 refers to contracts which have become 'impossible of performance or been otherwise frustrated'.

7 *Hirji Mulji v. Cheong Yue Steamship Co. Ltd* [1926] AC 497, 505, PC, *per* Lord Sumner.

8 Express terms not precluding frustration: *Metropolitan Water Board v. Dick, Kerr & Co.* [1918] AC 119, HL; and *Bank Line Ltd v. Arthur Capel & Co.* [1919] AC 435, HL; *Treitel* (12th edn, London, 2007), 19-073, 19-074.

9 '*The Great Peace*' [2002] EWCA Civ 1407; [2003] QB 679, at [74].

10 E. McKendrick (ed.), *Force Majeure and Frustration of Contract* (2nd edn, London, 1995), especially at 34; E. McKendrick, 'The Regulation of Long-Term Contracts in English Law', in J. Beatson and D. Friedmann (eds.), *Good Faith and Fault in Contract Law* (Oxford, 1995), 305, 323 ff; E. McKendrick, 'Force Majeure Clauses: The Gap between Doctrine and Practice', in A. Burrows and E. Peel (eds.), *Contract Terms* (Oxford, 2007), chapter 12; *Chitty on Contracts* (30th edn, London, 2008), 14-137 ff; E. McKendrick, *Contract Law* (8th edn, London, 2009), 14.9.

- (8) Long-term contracts, unless of fixed duration, are subject to an implied term enabling one party to give reasonable notice to the other that the contract will be terminated.

History

A. W. B. Simpson, 'Innovation in Nineteenth Century Contract Law' (1975) 91 LQR 247, at 269-73

D. Ibbetson, in F. D. Rose (ed.), *Consensus ad Idem: Essays in the Law of Contract in Honour of Guenter Treitel* (London, 1996), chapter 1 (for an earlier history)

Exceptional increases in expense

J. Beatson, 'Increased Expense and Frustration', in F. D. Rose (ed.), *Consensus ad Idem: Essays in the Law of Contract in Honour of Guenter Treitel* (London, 1996), 121

Adjustment of frustrated contracts: the Law Reform (Frustrated Contracts) Act 1943

E. McKendrick, 'Frustration, Restitution and Loss Adjustment', in A. Burrows (ed.), *Essays on Restitution* (Oxford, 1991), 147

Force majeure clauses

E. McKendrick (ed.), *Force Majeure and Frustration of Contract* (2nd edn, London, 1995), especially at 34

E. McKendrick, 'The Regulation of Long-Term Contracts in English Law', in J. Beatson and D. Friedmann (eds.), *Good Faith and Fault in Contract Law* (Oxford, 1995), 305, 323 ff

E. McKendrick, 'Force Majeure Clauses: The Gap between Doctrine and Practice', in A. Burrows and E. Peel (eds.), *Contract Terms* (Oxford, 2007), chapter 12

2. MAIN THREADS OF THE DOCTRINE

- 16.02** *Definition and genesis.* Lord Radcliffe gave the leading definition of the doctrine in *Davis Contractors Ltd v. Fareham Urban District Council* (1956) (for the facts of this case, see 16.09):¹¹

[F]rustration occurs whenever the law recognises that without default of either party a contractual obligation has become incapable of being performed because the circumstances in which performance is called for would render it a thing radically

¹¹ *Davis Contractors Ltd v. Fareham Urban District Council* [1956] AC 696, 729, HL, *per* Lord Radcliffe; considered in *Pioneer Shipping Ltd v. BTP Tioxide Ltd ('The Nema')* [1982] AC 724, 744, 751-2, HL; '*The Great Peace*' [2002] EWCA Civ 1407; [2003] QB 679, at [70].

different from that which was undertaken by the contract. *Non haec in foedera veni*. It was not this which I promised to do.

Blackburn J in *Taylor v. Caldwell* (1863) first acknowledged a general doctrine of frustration (for the facts, see 16.08).¹² This makes 'frustration' a doctrinal 'latecomer' within the common law system of contract. Before 1863, the general approach was very strict (although not quite absolute). The strict approach is evident from *Paradine v. Jayne* (1647).¹³

This was an action by Robert Paradine for three years' rent arrears, payable by William Jayne, the tenant of seventeen acres of land leased to him in 1637 for twenty-one years at a rent of £21 per year, in Bedminster, Bristol. The tenant attempted to defend himself from liability to pay rent for two and a half of these years, on the basis that Prince Rupert and his army had seized and occupied the land during the English Civil War. In his microscopic and remarkable examination of this case, Ibbetson suggests¹⁴ that the tenant had probably been unable to use the land during the relevant period for agricultural purposes because of the turmoil caused by the Civil War, which had undoubtedly affected this part of the countryside neighbouring Bristol. Nevertheless, the court rejected the defence, deciding that the tenant's obligation to pay rent was quite strict (for the possibility now that a lease might become frustrated, see 16.14 below).

Blackburn J's innovation in *Taylor v. Caldwell* (1863)¹⁵ involved a bold generalisation: for he pieced together a general doctrine of frustration, drawing upon three fragments, these being extreme situations where the common law already excused a contractual party for his non-performance. These three fragments were: (1) a contracting party's death in a contract of personal services (his spiritual survival not being enough, as where the piano recitalist dies halfway through the concert); (2) destruction of specific goods after property has passed to the buyer; (3) bailment where goods are destroyed without the bailor's fault.¹⁶ Blackburn J's generalisation enabled him to fashion a doctrine of frustration capable of extending to destruction of a building or immovable property (in the case of *Taylor v. Caldwell*, loss of the music hall).

The four key points in the history of the doctrine of frustration were attractively chronicled by Mustill LJ in *FC Shepherd v. Jerrom* (1987) as follows:¹⁷

[1.] The starting point was the principle laid down by *Paradine v. Jayne* (1647) Aleyn 26 [see 16.02 above] that a party who had created a duty upon himself was bound to perform it or pay damages even if his nonperformance was brought about by a supervening event beyond his control ...

12 (1863) 3 B & S 826; 122 ER 309; A. W. B. Simpson, (1975) 91 LQR 247, 269–73; C. MacMillan, in C. Mitchell and P. Mitchell (eds.), *Landmark Cases in the Law of Contract* (Oxford, 2008), 167 ff.

13 (1647) Aleyn 26; 82 ER 897 (Court of King's Bench); D. Ibbetson, in F. D. Rose (ed.), *Consensus ad Idem: Essays on the Law of Contract in Honour of Guenter Treitel* (London, 1996), chapter 1.

14 D. Ibbetson, in F. D. Rose (ed.), *Consensus ad Idem: Essays on the Law of Contract in Honour of Guenter Treitel* (London, 1996), chapter 1.

15 (1863) 3 B & S 826; 122 ER 309; A. W. B. Simpson, (1975) 91 LQR 247, 269–73.

16 G. H. Treitel, *Frustration and Force Majeure* (2nd edn, London, 2004), 2–022.

17 [1987] QB 301, 321–2, CA.

[2.] In *Taylor v. Caldwell* (1863) 3 B & S 826 [see 16.02 above], the law moved a great step forward when the Court of Queen's Bench recognised that the contract could be discharged by the failure of an implied condition precedent, and that in appropriate circumstances a condition could be implied to the effect that a particular person or thing should continue to exist ...

[3.] In due course, the implied condition was extended beyond cases of outright impossibility to embrace those where the supervening event put an end, in a business sense, to the engagement of the parties and frustrated the object of that engagement. This expression seems first to have appeared in *Jackson v. Union Marine Insurance Co. Ltd* (1874) LR 10 CP 125, 145 ... [where] the concept of frustration of the adventure [see 16.12 and 16.13 below] became the touchstone of the type of event which would discharge the promisor.

[4.] More recently, the doctrine has been modified as regards both rationalisation and terminology. The idea of the implied term that the promisor's obligation will be capable of performance without alterations which frustrate the adventure is no longer in favour. Since *Davis Contractors Ltd v. Fareham Urban District Council* [1956] AC 696 [see 16.03 and 16.09 below] the procedure has been to construe the contract and then see whether if the contract is enforced in its literal sense the performance in the changed circumstances will involve a radically different thing from that which was contemplated by the contract, so construed.

16.03 *Frustration does not rest on an implied term.* *Taylor v. Caldwell* (1863)¹⁸ remains good law, but its conceptual basis has changed. In 1863, Blackburn J had based the contract's cessation on an implied term: '[B]ut that excuse is by law implied, because from the nature of the contract it is apparent that the parties [had decided to] contract on the basis of the continued existence of the particular person or chattel.'¹⁹ However, Blackburn J did not mean to suggest that the parties had themselves implicitly agreed on this excuse. Even so, the language of 'implied terms' was later regarded as unhelpful, and the courts now accept that it would be a fiction to base the doctrine of frustration on an implied term. This is because the parties do not truly share a tacit consensus concerning the impact of the relevant event. Instead, frustration rests on a doctrine of law, and this is rooted in the need to release the parties from extreme and unavoidable difficulty or impossibility. As Lord Radcliffe explained in *Davis Contractors Ltd v. Fareham Urban District Council* (1956):²⁰

[The implied term theory] is in line with the tendency of English courts to refer all the consequences of a contract to the will of those who made it. But there is something of a logical difficulty in seeing how the parties could even impliedly have provided for something which *ex hypothesi* they neither expected nor foresaw; and the ascription of frustration to an implied term of the contract has been criticised as obscuring the true

18 (1863) 3 B & S 826; 122 ER 309; D. J. Ibbetson, *A Historical Introduction to the Law of Obligations* (Oxford, 1999), 224.

19 *Ibid.*

20 [1956] AC 696, HL.

action of the court which consists in applying an objective rule of the law of contract to the contractual obligations that the parties have imposed upon themselves.

Lord Denning MR remarked in *'The Eugenia'* (1964):²¹

It was originally said that the doctrine of frustration was based on an implied term. In short, that the parties, if they had foreseen the new situation, would have said to one another: 'If that happens, of course, it is all over between us.' But the theory of an implied term has now been discarded by everyone, or nearly everyone, for the simple reason that it does not represent the truth. The parties would not have said: 'It is all over between us.' They would have differed about what was to happen. Each would have sought to insert reservations or qualifications of one kind or another.

And consider the wry comment of a Scottish judge in *James Scott & Sons Ltd v. Del Sel* (1922):

A tiger has escaped from a travelling menagerie. The milkgirl fails to deliver the milk. [If the milkman is exonerated from failure to deliver] it would hardly seem reasonable to base that exoneration on the ground that 'tiger days excepted' must be held as if written into the contract.²²

16.04 *Mistake or frustration? A question of timing.* If the event alleged to produce impossibility or a radically different situation from that envisaged by the parties *antedates the contract*, the relevant doctrine is mistake (on which see chapter 10).²³

For example, in *Griffith v. Brymer* (1903), a 'room with a view' had been booked after the Coronation of Edward VII had already been postponed.²⁴ Neither party realised that this postponement had already been announced. The contract was held to be void for mistake. The converse situation (where the contract was formed before the Coronation's postponement, and so gave rise to frustration) is examined at 16.13 below in the discussion of *Krell v. Henry* (1903).

Amalgamated Investment & Property Co. Ltd v. John Walker & Sons Ltd (1977)²⁵ also illustrates that even a short interval can be enough to separate mistake and frustration. The Court of Appeal held that a contract for the purchase of an industrial property had already been formed before the planning authorities made a final decision to list the building as possessing special architectural or historical interest. Because the planning decision was made after the contract's formation, this could not be a case of mistake. Instead, it fell potentially for consideration as an instance of frustration. In fact, the frustration argument also failed because the listing did not fundamentally alter the contract's essential nature: it remained a transaction giving the purchaser title to the relevant land.

21 [1964] 2 QB 226, 238, CA; see, further, 16.06 on this case.

22 1922 SC 592, 597.

23 The mistake doctrine is extensively analysed in *'The Great Peace'* [2002] EWCA Civ 1407; [2003] QB 679.

24 *Griffith v. Brymer* (1903) TLR 434, Wright J; on which *'The Great Peace'* [2002] EWCA Civ 1407; [2003] QB 679, at [67].

25 [1977] 1 WLR 164, CA.

This was so, even though the listing had been commercially disastrous for the purchaser, who had wished to develop the site. To repeat, the doctrine of frustration is narrow in compass (see further on this case 16.05, concerning allocation of risk).

- 16.05** *Risk allocated to one party.* Frustration operates only if the contract contains neither an express²⁶ nor an implied allocation of the relevant risk to one of the parties. As Lord Simon explained in *National Carriers Ltd v. Panalpina (Northern) Ltd* (1981):²⁷

[T]he doctrine [of frustration] has been described as a ‘device’ for doing justice between the parties when they themselves have failed either wholly or sufficiently to provide for the particular event or events which have happened. The doctrine is principally concerned with the incidence of risk – who must take the risk of the happening of a particular event especially when the parties have not made any or any sufficient provision for the happening of that event? When the doctrine is successfully invoked it is because in the event which has happened the law imposes a solution, casting the incidence of that risk on one party or the other as the circumstances of the particular case may require, having regard to the express provisions of the contract into which the parties have entered.

And, as Lord Phillips CJ said in *‘The Great Peace’* (2003):²⁸

In considering whether performance of the contract is impossible, it is necessary to identify what it is that the parties agreed would be performed. This involves looking not only at the express terms, but [looking also] at any implications that may arise out of the surrounding circumstances. In some cases it will be possible to identify details of the ‘contractual adventure’ which go beyond the terms that are expressly spelt out, in others it will not.

He added:²⁹

In the *William Sindall* case (1994) Hoffmann LJ commented that such allocation of risk can come about by rules of general law applicable to contract, such as ‘caveat emptor’ in the law of sale of goods or the rule that a lessor or vendor of land does not impliedly warrant that the premises are fit for any particular purpose, so that this risk is allocated by the contract to the lessee or purchaser.

When determining how risk should be implicitly allocated, the court must consider the relevant contract sensitively, with full awareness of its context. As Rix LJ said in *‘The Sea Angel’* (2007):³⁰

²⁶ For cases where express terms were construed not to preclude frustration, see *Metropolitan Water Board v. Dick, Kerr & Co.* [1918] AC 119, HL; and *Bank Line Ltd v. Arthur Capel & Co.* [1919] AC 435, HL; *Treitel* (12th edn, London, 2007), 19-073, 19-074.

²⁷ [1981] AC 675, 712, HL, *per* Lord Simon.

²⁸ *‘The Great Peace’* [2002] EWCA Civ 1407; [2003] QB 679, at [74].

²⁹ *Ibid.*, at [81], citing *William Sindall plc v. Cambridgeshire County Council* [1994] 1 WLR 1016, 1035, CA.

³⁰ *Edwinton Commercial Corporation v. Tsaviris Russ Ltd (‘The Sea Angel’)* [2007] EWCA Civ 547; [2007] 2 Lloyd’s Rep 517, at [111].

Since the subject matter of the doctrine of frustration is contract, and contracts are about the allocation of risk, and since the allocation and assumption of risk is not simply a matter of express or implied provision but may also depend on less easily defined matters such as ‘the contemplation of the parties’, the application of the doctrine can often be a difficult one. In such circumstances, the test of ‘radically different’ is important: it tells us that the doctrine is not to be lightly invoked; that mere incidence of expense or delay or onerousness is not sufficient; and that there has to be, as it were, a break in identity between the contract as provided for and contemplated and its performance in the new circumstances.

An example of the courts imputing a risk to a party is *Amalgamated Investment & Property Co. Ltd v. John Walker & Sons Ltd* (1977),³¹ where the Court of Appeal held that a purchaser of land takes the risk that, subsequent to the contract’s formation, the property might become listed as a building of special architectural or historical interest. No frustration arose on these facts, even though the listing decision had prevented the purchaser from developing the site as he had intended.

- 16.06** *Foreseeability (and the connection with risk allocation)*. If an event is foreseeable, it is likely, although not inevitable, that the event will not be a frustrating event.³² The better view is that foresight and foreseeability are not free-standing impediments to frustration. Instead, they are factors concerning the issue whether one party has impliedly assumed the risk of the relevant event’s occurrence.

In the *Maritime National* case (1935),³³ the defendant hired a trawler, the *St Cuthbert* from the claimant. The defendant had four other trawlers. As the parties foresaw, the trawlers could only operate under government licence. The defendant received only three licences, although he had applied for five. He then chose to use these licences for three of his vessels. He chose not to license the *St Cuthbert*. The owner sued the defendant for the hire charges, but the latter argued that the contract of hire had been frustrated by his inability to obtain sufficient licences. The Canadian courts held that the defendant’s frustration plea should fail. This was primarily because the ‘event’ was plainly foreseeable and not an extraneous calamity. The Privy Council accepted this point, but Lord Wright deftly explained it as a conclusion based upon risk rather than foreseeability *simpliciter*.³⁴

[The Canadian Supreme Court] held that there was in this case no discharge of the contract for one or both of two reasons. In the first place they thought that the appellants when they renewed the charter in 1932 were well informed of the legislation, and when they renewed the charter at a reduced rate and inserted no protecting clause in this regard, must be deemed to have taken the risk that a licence would not be granted. They also thought that if there was frustration of the

31 [1977] 1 WLR 164, CA.

32 See the discussion later in this paragraph of Lord Denning’s remarks in *Ocean Tramp Tankers Corporation v. V/O Sovfracht* (*‘The Eugenia’*) [1964] 2 QB 226, CA; cf C. Hall, (1984) 4 LS 300 (proposing a recklessness basis).

33 *Maritime National Fish Ltd v. Ocean Trawlers Ltd* [1935] AC 524, PC.

34 [1935] AC 524, 526, PC.

adventure, it resulted from the deliberate act of the appellants in selecting the three trawlers for which they desired licences to be issued.

This 'better view' is traceable to Lord Denning MR's discussion in *'The Eugenia'* (1964), where he said:³⁵

It has frequently been said that the doctrine of frustration only applies when the new situation is 'unforeseen' or 'unexpected' or 'uncontemplated', as if that were an essential feature. But it is not so. The only thing that is essential is that the parties should have made no provision for it in their contract. The only relevance of it being 'unforeseen' is this: If the parties did not foresee anything of the kind happening, you can readily infer they have made no provision for it: whereas, if they did foresee it, you would expect them to make provision for it.

He continued:

But cases have occurred where the parties have foreseen the danger ahead, and yet made no provision for it in the contract. Such was the case in the Spanish Civil War when a ship was let on charter to the republican government. The purpose was to evacuate refugees. The parties foresaw that she might be seized by the nationalists. But they made no provision for it in their contract. Yet, when she was seized, the contract was frustrated, see *WJ Tatem Ltd v. Gamboa* [1939] 1 KB 132. So here [in *'The Eugenia'*] the parties foresaw that the canal might become impassable: it was the very thing they feared. But they made no provision for it. So there is room for the doctrine to apply if it be a proper case for it.

As Lord Denning MR explained, the true question is whether one of the parties expressly or impliedly bears the risk of the relevant event. In light of these remarks, the true position can be summarised as follows:

- (1) The rule of public policy that a contract ceases to bind once it becomes illegal is one which terminates the contract irrespective of questions of foresight or foreseeability; trading with the enemy is one such type of illegality; so parties contracting against the imminent outbreak of war will find their contract frustrated if that rule of illegality applies to their contract.
- (2) A foreseeable event (even though not in fact foreseen) can preclude frustration, provided the risk is not too remote a possibility. The question is whether the event's occurrence is a risk implicitly allocated to one party. If it is not, there remains room for frustration to arise.
- (3) If an event (other than illegality: see above) is foreseen, it becomes likely, but not inevitable, that this is a risk borne by a party. If so, that event will not frustrate the contract.

³⁵ *'The Eugenia'* [1964] 2 QB 226, CA; C. Hall, (1984) 4 LS 300 (proposing a recklessness basis).

- (4) The final possibility is that the parties actually discuss what to do about a possible event (other than illegality: see above). If they fail to reach a consensus on how the risk is to be allocated, the law remains free to intervene; the court can determine how the risk should be allocated, or whether in fact the risk is not borne by either party. In the latter situation, frustration remains possible if the event is sufficiently serious and neither party was at fault in the relevant circumstances.

It is also instructive to note Rix LJ's more recent discussion of these matters in *'The Sea Angel'* (2007):³⁶

In a sense, most events are to a greater or lesser degree foreseeable. That does not mean that they cannot lead to frustration. Even events which are not merely foreseen but made the subject of express contractual provision may lead to frustration: as occurs when an event such as a strike, or a restraint of prices, lasts for so long as to go beyond the risk assumed under the contract and to render performance radically different from that contracted for. However ... the less that an event, in its type and its impact, is foreseeable, the more likely it is to be a factor which, depending on other factors in the case, may lead on to frustration.

3. THE SCOPE OF FRUSTRATION

16.07 The contract will be frustrated if, subsequent to the contract's formation, performance of the contract becomes illegal, either because a statutory or other legal change occurs or because a subsisting source of prohibition is newly implemented (for the situation where the contract is illegal from its inception, or one or more party chooses to perform it in an illegal fashion, see chapter 20). It is not possible to contract out of supervening illegality if to do so would be contrary to public policy.³⁷ Examples of supervening illegality are:

- (1) In *Metropolitan Water Board v. Dick, Kerr & Co.* (1918) (also at 16.12), a contract, formed in 1914, required the builder to construct a reservoir within six years.³⁸ However, in 1916, an order was made under the Defence of the Realm legislation requiring the contractors to stop work. Although the contract provided for an extension of time, the House of Lords held that the extent of interruption here was so great that the contract could no longer be regarded as the same, price and labour costs having changed significantly.³⁹ And so the contract had become frustrated by reason of supervening illegality.
- (2) In the *Fibrosa* (1943) case,⁴⁰ a contract for the supply by a British company of machinery to a port in Poland was frustrated when the German forces took control

³⁶ *Edwinton Commercial Corporation v. Tsavlis Russ Ltd ('The Sea Angel')* [2007] EWCA Civ 547; [2007] 2 Lloyd's Rep 517, at [127].

³⁷ *Ertel Bieber & Co. v. Rio Tinto Co. Ltd* [1918] AC 260, 273, HL.

³⁸ *Metropolitan Water Board v. Dick, Kerr & Co.* [1918] AC 119, HL.

³⁹ *Ibid.*, at 130.

⁴⁰ [1943] AC 32, 39–40, HL.

of Poland. In this situation, the contract became illegal because its performance would entail the supplier trading with the enemy, a clear-cut instance of illegality. This case is further examined at 16.21 and 18.53.

- (3) In *Gamerco SA v. ICM/Fair Warning (Agency) Ltd* (1995),⁴¹ a contract for the promotion of a rock concert in Madrid foundered when the chosen venue was declared unfit for public use, because of crumbling construction work (technically, a revocation of a permit to use the venue for public use). The contract was subject to English law, and the municipal prohibition was based on Spanish law. The contract was clearly frustrated (on the consequence of this, see the discussion of this case at 16.24).

16.08 *Physical impossibility.* Contracts for the performance of personal services are frustrated if, before completion of the relevant task, the performer is incapacitated (without his fault) by illness, or becomes mentally incapable of acting, or dies. Another example of ‘physical impossibility’ is when the physical subject matter of the proposed performance has been destroyed or it has disappeared without any default by the parties. This is illustrated by *Taylor v. Caldwell* (1863)⁴² (the decision which established the modern doctrine):

The defendant in *Taylor v. Caldwell* (1863) had agreed to make available to the claimant a music hall and gardens for four days. The claimant agreed on these days to provide artistes who would entertain. It was a kind of joint venture. Performance of the contract was frustrated by a fire which gutted the music hall. This fire was not attributable to the fault, or breach, of either party. The claimant claimed £58 as expenses, mostly advertising costs. But the court rejected the claim. It declared the contract had ended once the music hall was consumed by the flames. Therefore, if the defendant had counter-claimed for unpaid hire, that claim would also have failed.

16.09 *Difficulty and ‘impracticability’: no frustration.* The fact that a contract becomes more difficult to perform is not enough to constitute frustration. English law’s insistence on commercial discipline is of great commercial significance. The leading discussion is *Davis Contractors Ltd v. Fareham Urban District Council* (1956).⁴³

This case concerned a contract to build seventy-eight houses for a price of approximately £94,000. The work was to be completed within eight months. Labour shortages slowed down the work so that it took twenty-two months. Such shortages were not unforeseeable in the chaotic post-war period. The cost of doing the work rose to approximately £115,000. The builder managed to complete the work. He then argued that the contract had become frustrated by operation of law. This was a tactical argument in the sense that he wanted to claim more money for the job he had completed. The frustration plea was being used to contend that, from the date of discharge, his work should be remunerated at the higher

41 [1995] 1 WLR 1226, Garland J.

42 (1863) 3 B & S 826; 122 ER 309.

43 [1956] AC 696, HL.

market rate. This would be in accordance with a *quantum meruit*, an extra-contractual and restitutionary claim. In fact, the arbitrator, having found that the contract had been frustrated, had awarded the builder such an extra payment. But the House of Lords rejected this award as wrong in law. Instead, it held that there was no scope on these facts for finding frustration because these changes were not drastic enough to satisfy that doctrine. And so the builder remained bound by the original price.

The decision in *Davis Contractors Ltd v. Fareham Urban District Council* (1956) is tough but commercially sound. This was not an extreme change of situation. The cost of the work had increased by less than 25 per cent. This increase in cost unfortunately eliminated the builder's profit margin: the actual cost of building exceeded the agreed price for the job. But this made no difference. This risk is borne by the builder. The contract cannot be dissolved just because 'the going gets tough'. It is not enough that a party's profit margin is reduced or that the deal becomes an economic disaster for this party. As Treitel acknowledges,⁴⁴ English law is clearly committed to the proposition that mere increases in hardship or expense do not constitute grounds of frustration. It might even be the law that no increase in expense can ever amount to frustration, no matter how severe the hardship to the affected party. Although Beatson⁴⁵ has suggested that a safety valve should be created for really extreme situations of increased difficulty, there is abundant judicial authority which is contrary to that suggestion. For example, Lord Loreburn said in *Tennants (Lancashire) Ltd v. CS Wilson & Co.* (1917):⁴⁶

[T]he argument that a man can be excused from performance of his contract when it becomes 'commercially' impossible seems to be a dangerous contention which ought not to be admitted unless the parties have plainly contracted to that effect.

In *British Movietonews Ltd v. London District Cinemas* (1952),⁴⁷ Lord Simon said:

[T]he parties to an executory contract are often faced, in the course of carrying it out, with a turn of events which they did not at all anticipate – a wholly abnormal rise or fall in prices, a sudden depreciation of currency, an unexpected obstacle to execution or the like. Yet this does not of itself affect the bargain they have made.

Lord Radcliffe said in the *Davis* case (1956):

[I]t is not hardship or inconvenience or material loss itself which calls the principle of frustration into play.⁴⁸

⁴⁴ Treitel (12th edn, London, 2007), 19-032 to 19-040.

⁴⁵ J. Beatson, 'Increased Expense and Frustration', in F. D. Rose (ed.), *Consensus ad Idem: Essays on the Law of Contract in Honour of Guenter Treitel* (London, 1996), 121; on 1920s German hyper-inflation, see W. Lorenz, in J. Beatson and D. Friedmann (eds.), *Good Faith and Fault in Contract Law* (Oxford, 1995), 357, 365 ff.

⁴⁶ [1917] AC 495, 510, HL.

⁴⁷ [1952] AC 166, 185, HL.

⁴⁸ *Davis Contractors Ltd v. Fareham Urban District Council* [1956] AC 696, 729, HL, *per* Lord Radcliffe; considered in 'The Great Peace' [2002] EWCA Civ 1407; [2003] QB 679, at [70]; *Pioneer Shipping Ltd v. BTP Tioxide Ltd ('The Nema')* [1982] AC 724, 744, 751-2, HL.

Lord Denning MR said in *'The Eugenia'* (1964):⁴⁹

[T]he fact that it has become more onerous or more expensive for one party than he thought is not sufficient to bring about a frustration. It must be more than merely more onerous or more expensive. It must be positively unjust to hold the parties bound.

The strict approach of English law sends a clear message to negotiating parties, who must appreciate that they will not be able to escape their bargains except in extreme circumstances where the contract becomes impossible or illegal, or its very foundation has been annihilated by a change of circumstance (on that unusual possibility, see 16.13). Provision can be made in the contract, by insertion of *force majeure* or hardship clauses, to achieve a consensual modification of this strict regime. A *force majeure* clause declares when a party will be released from his obligations, or excused from liability for default, by reason of freak and excusable supervening events⁵⁰ (see also 16.19, for reference to the clause in *'The Super Servant Two'* (1990)). But, in *Thames Valley Power Ltd v. Total Gas & Power Ltd* (2005),⁵¹ Clark J held that even a *force majeure* clause will not exonerate an energy supplier, who has agreed to supply energy under a fifteen-year contract, even though there has been a very significant increase in the wholesale price. The supply of energy remained possible, even though increases in the costs of supply had rendered the contract very unattractive to the energy company.

Admittedly, the austere approach of English law is in contrast to the recommendations contained in the 'soft law' codes of PECL, the *Principles of European Contract Law*, and UNIDROIT's *Principles of International Commercial Contracts* (2004). Article 6:111 ('Change of Circumstances') of PECL, the *Principles of European Contract Law*, states:

- (1) A party is bound to fulfil its obligations even if performance has become more onerous, whether because the cost of performance has increased or because the value of the performance it receives has diminished.
- (2) If, however, performance of the contract becomes excessively onerous because of a change of circumstances, the parties are bound to enter into negotiations with a view to adapting the contract or terminating it, provided that:
 - (a) the change of circumstances occurred after the time of conclusion of the contract,
 - (b) the possibility of a change of circumstances was not one which could reasonably have been taken into account at the time of conclusion of the contract, and

49 [1964] 2 QB 226, 239, CA.

50 E. McKendrick (ed.), *Force Majeure and Frustration of Contract* (2nd edn, London, 1995), especially at 34; E. McKendrick, 'The Regulation of Long-Term Contracts in English Law', in J. Beatson and D. Friedmann (eds.), *Good Faith and Fault in Contract Law* (Oxford, 1995), 305, 323 ff; E. McKendrick, 'Force Majeure Clauses: The Gap between Doctrine and Practice', in A. Burrows and E. Peel (eds.), *Contract Terms* (Oxford, 2007), chapter 12; *Chitty on Contracts* (30th edn, London, 2008), 14-137 ff.

51 [2005] EWHC 2208 (Comm); [2006] 1 Lloyd's Rep 441.

(c) the risk of the change of circumstances is not one which, according to the contract, the party affected should be required to bear.

(3) If the parties fail to reach agreement within a reasonable period, the court may:

- (a) end the contract at a date and on terms to be determined by the court; or
- (b) adapt the contract in order to distribute between the parties in a just and equitable manner the losses and gains resulting from the change of circumstances.

In either case, the court may award damages for the loss suffered through a party refusing to negotiate or breaking off negotiations contrary to good faith and fair dealing.

Article 6.2.3⁵² of UNIDROIT's *Principles of International Commercial Contracts* (2004) differs from the PECL provision: the UNIDROIT provision prescribes a regime for voluntary negotiation to address a problem of 'hardship' (sensibly confined (see Article 6.2.2) to matters not allocated as risks under the contract and beyond the disadvantaged party's control). If that negotiation does not produce a solution 'within a reasonable time', either party can 'resort to court'. 'If the court finds hardship it may, if reasonable, (a) terminate the contract at a date and on terms to be fixed, or (b) adapt the contract with a view to restoring its equilibrium.'

16.10 *Supply of generic goods: an uphill struggle to excuse non-supply.* A wholesale seller owes a strict (although not quite an absolute: see 16.11) duty to procure goods from sources 'further up the chain': he will seldom succeed in showing that the stated source has dried up entirely so that it was impossible to obtain a supply. *Blackburn Bobbin v. TW Allen* (1918) illustrates the strict position:⁵³

The defendant had agreed to sell the claimant a certain quantity of Finnish timber to be delivered between June and November 1914. Timber merchants did not keep stocks of Finnish timber in this country but instead shipped timber directly from Finland to meet such large contracts. At the outbreak of war in August 1914, the defendants had not made any deliveries under the contract. It later became impossible to import timber because German warships were blocking the Baltic.

The Court of Appeal, however, held that the contract had not been frustrated. Continuance of the usual shipping arrangements (these being unknown to the claimants) was not fundamental to the existence of the contract. In other words, having contracted in unqualified terms, the seller took the risk of not being able to obtain the goods needed to perform the contract. A clause such as 'assuming that imports from Finland remain possible' would have changed the position.

52 2nd edn, Rome, 2004; see M. J. Bonell (ed.), *The UNIDROIT Principles in Practice: Case Law and Bibliography on the UNIDROIT Principles of International Commercial Contracts* (2nd edn, Ardsley, NY, 2006), 333 ff; S. Vogenauer and J. Kleinheisterkamp (eds.), *Commentary on the UNIDROIT Principles of International Commercial Contracts* (Oxford, 2009), 722.

53 [1918] 2 KB 467, CA.

Similarly, in *CTI Group Inc. v. Transclear SA* (2008), the Court of Appeal confirmed that a supplier of generic goods normally assumes liability towards the buyer in respect of the supplier's inability to procure goods further up the supply chain:⁵⁴ the fact that the supplier is himself denied supply does not exonerate him. Moore-Bick LJ explained:⁵⁵

[I]n the absence of some exceptional supervening event, such a contract will not be frustrated simply by a failure on the part of the ultimate supplier to make goods available for delivery. The reason for that is not far to seek: it is implicit in a contract of this kind that the seller will either supply the goods himself or (more likely) will make arrangements, directly or indirectly, for the goods to be supplied by others. In other words, he undertakes a personal obligation to procure the delivery of contractual goods and thereby takes the risk of his supplier's failure to perform.

- 16.11 *Successful plea of frustration: supply unavoidably blocked from nominated foreign source.* Frustration might occur if the sole foreign supplier has placed an embargo on all supplies of the relevant commodity *from the stipulated foreign source*. *Société Cooperative Suisse des Céréales et Matières Fourragères v. La Plata Cereal Company SA* (1946)⁵⁶ illustrates the case of immediate import from a stipulated source (compare the *Blackburn Bobbin* case in the paragraph, where the contract did not mention that supply had to be *imported from Finland*):

The *Société Cooperative Suisse* case (1946) concerned two contracts in December 1944 and January 1945 respectively for the sale of Plate maize for shipment from Buenos Aires, the shipments to begin during the period 16 May to 1 June 1945. On 30 April and 2 May 1945, the Argentine government issued two decrees which provided that all maize destined for export must be purchased exclusively from the Agricultural Products Regulating Board, but that Board did not have goods of the contractual description which they were willing to sell for export before 30 June 1945. Morris J held that the contract had been frustrated:⁵⁷

[T]he basis of the contract did become overthrown ... There was ... a *de facto* prohibition which prevented the sellers from exporting. They were by law prohibited from exporting any maize that they had not purchased from the Argentine Agricultural Products Regulating Board, and that Board had no maize which they were willing to sell ... The new conditions created by the changes in the law fundamentally altered the situation.

- 16.12 *Delay: 'it all depends'.* Whether delay operates to frustrate the relevant contract will depend on the context. Thus, the House of Lords in *'The Nema'* restored the arbitrator's decision that strikes had caused delay sufficient to frustrate a charterparty for the year 1979. As Lord Roskill explained in that case, it is a question of 'degree'.⁵⁸

54 [2008] EWCA Civ 856.

55 *Ibid.*, at [14] and [23].

56 (1946) 80 Lloyd's Rep 530, Morris J.

57 *Ibid.*, at 543, col. 1.

58 *Pioneer Shipping Ltd v. BTP Tioxide Ltd ('The Nema')* [1982] AC 724, 752, HL, *per* Lord Roskill.

Delay was found to be *insufficient* in the following cases:

- (1) In the *Davis Contractors* case (1956)⁵⁹ (16.09), a building contract expected to last eight months in fact took twenty-two months. But this delay did not amount to frustration.
- (2) In *'The Eugenia'* (1964), a voyage which was expected to last 108 days (the originally intended route from the Black Sea to India was to go via the Suez Canal) in fact lasted 138 days (it was necessary to go the long way round, via the Cape of Good Hope), but the Court of Appeal held that this was insufficient to constitute frustration.⁶⁰
- (3) In *'The Sea Angel'* (2007), a vessel, hired for up to twenty days to assist in a salvage operation, was prevented from leaving its port by the Pakistani port authority until payment had been made for the loss caused by pollution (oil leaking from a tanker which the salvage vessel had been hired to rescue).⁶¹ Extricating the salvage vessel from this situation prolonged the transaction by over three months (as mentioned, the anticipated length of the salvage hire was merely twenty days). The Court of Appeal held that this delay did not involve frustration and that its occurrence and duration fell within the scope of the risk borne by the charterer. That party was, therefore, liable to pay hire at the agreed daily rate.

Delay was found to be *sufficient* in the following cases:

- (1) In *Metropolitan Water Board v. Dick, Kerr & Co.* (1918) (also at 16.07), a building contract was held to have been frustrated because of a severe delay.⁶² This was an agreement for construction of a reservoir within six years. The work was then affected by a wartime government order which required the contractor to stop work and to sell their construction plant. The House of Lords concluded that the contract had been frustrated even though the contract provided for an extension of time in the event of delays 'howsoever occasioned'. It was held that those words, although literally wide enough, should not be construed as covering the drastic 'event' in question.
- (2) In *Jackson v. Union Marine Insurance Co. Ltd* (1874),⁶³ P's ship had been chartered to carry rails from Newport in Wales to San Francisco. The ship ran aground on its way from Liverpool to Newport, where loading was to take place. Repairs took nine months. In the meantime, X, the charterer, had hired another vessel, and decided not to pay P. P successfully claimed against his insurer for this loss of payment. The court held that, if P had sued X for payment of the freight, X could have pleaded

⁵⁹ [1956] AC 696, HL.

⁶⁰ [1964] 2 QB 226, CA.

⁶¹ *Edwinton Commercial Corporation v. Tsavlis Russ Ltd ('The Sea Angel')* [2007] EWCA Civ 547; [2007] 2 Lloyd's Rep 517, at [132] and [133].

⁶² [1918] AC 119, HL.

⁶³ (1874) LR 10 CP 125, Exchequer Chamber.

that the venture had been radically changed in view of the delay, and that the contract for carriage had been frustrated (see also 16.13).

16.13 Frustration of the venture or purpose: exceptional source of frustration. This category of frustration is seldom satisfied in practice (Mustill LJ in *FC Shepherd v. Jerrom* (1987) noted⁶⁴ that this concept seems to have appeared first in *Jackson v. Union Marine Insurance Co. Ltd* (1874): see 16.12).⁶⁵ An unusual instance is *Krell v. Henry* (1903), in which the hire of a room for one day overlooking the ceremonial Coronation procession of King Edward VII had been frustrated because the event had to be postponed when the King fell ill.⁶⁶ It was clear that the hire was for this purpose: the licensee could not sensibly be expected to languish in this room if the procession did not take place that day. The risk that the Coronation would be postponed could not fairly be allocated to the licensee. Vaughan-Williams LJ said:⁶⁷

[I do not think that the frustration doctrine] is limited to cases in which the event causing the impossibility of performance is the destruction or non-existence of some thing which is the subject matter of the contract or of some condition or state of things expressly specified as a condition of it ...

[Y]ou first have to ascertain, not necessarily from the terms of the contract, but, if required, from necessary inferences, drawn from surrounding circumstances recognised by both contracting parties, what is the substance of the contract, and then to ask the question whether that substantial contract needs for its foundation the assumption of the existence of a particular state of things.

If it does, this will limit the operation of the general words, and in such a case, if the contract becomes impossible of performance by reason of the non-existence of the state of things assumed by both contracting parties as the foundation of the contract, there will be no breach of the contract thus limited.

Krell v. Henry (1903) was distinguished by the Court of Appeal in *Herne Bay Steam Boat Co. v. Hutton* (1903). In the latter case, the ‘foundation’ of the contract had not wholly disappeared. Indeed, a large part of it remained.⁶⁸

The *Herne Bay Steam Boat* case concerned the commercial hire of a craft to be offered to members of the public so that, on payment, they could inspect the great naval review at Spithead. These events were to take place after the Coronation of Edward VII. The Court of Appeal held that his illness, and the postponement of the Coronation, did not render the

64 [1987] QB 301, 322, CA.

65 (1874) LR 10 CP 125, 145.

66 [1903] 2 KB 740, CA (Lord Wright in the *Maritime National Fish* case, [1935] AC 524, 529, PC, noting the exceptional nature of *Krell v. Henry*).

67 [1903] 2 KB 740, 749, CA.

68 [1903] 2 KB 683, CA.

contract of hire a 'complete waste of time' (to use modern parlance). And so there was no frustration. The King's absence at the review did not destroy the public's opportunity to see the magnificent array of warships at anchor.

This decision is sound. The King's presence would have enhanced the sense of occasion (because he would have been recently crowned). But his absence did not turn the naval review into a 'non-event'. It would perhaps have been different if the purpose of the hire had been specifically advertised in these terms: 'Vessel available for hire during King's review of the Fleet'. However, objectively, this was not the sole or predominant purpose of the hire on the facts of the case. The risk of slight public disappointment (and consequently a reduction in the public's interest in trips to view the fleet) was rightly allocated to the party who hired the craft.

It is submitted that *Krell v. Henry* and the *Herne Bay Steam Boat* case, although divergent in their results, are both soundly decided. *Krell v. Henry* shows that a contract can be frustrated even though it has not become illegal to perform and even though the contracting parties and the physical subject matter of the contract remain intact. Exceptionally, the *abstract platform* of the contract can disappear, rendering physical performance a hollow and futile activity. But it is also necessary to show that the risk of this disappointment cannot be reasonably imputed to the disappointed party (the licensee in *Krell v. Henry*; compare the hapless spectator at Lord's cricket ground who enjoys only ten overs and one ball⁶⁹ of 'live action', whereupon the rest of the day is rained off or play stops for 'bad light'). By contrast, the *Herne Bay Steam Boat* case shows that such abstract 'frustration of the venture' will not occur if only *part* of the anticipated contractual satisfaction has been removed by the relevant supervening change of circumstance, as opposed to all or most of it.

- 16.14 *Leases*: The House of Lords in *National Carriers Ltd v. Panalpina (Northern) Ltd* (1981) held that leases could be frustrated (although this will be quite exceptional).⁷⁰ It would indeed be anomalous if this type of contract were not subject to the 'general' doctrine of frustration.

National Carriers Ltd v. Panalpina (Northern) Ltd (1981) concerned a ten-year lease of a warehouse to the defendant. The only access to the warehouse was by a street. After five years of the term had elapsed, the local authority closed that street, for roughly eighteen months. This closure was necessary because a building opposite had been discovered to be in a dangerously derelict state. The landlord sought to recover unpaid rent. The defendants claimed that the lease had been frustrated. The House of Lords noted first that frustration is a possibility in the case of leases, but not on these facts: the period of sterilised use in this case was too short, considering the overall length of the lease and the fact that normality would

69 At Test matches (cricket), gate-money is refunded only if a specified number of overs are not played on the relevant day.

70 [1981] AC 675, HL.

return for the final three years of the lease, to constitute a radical deprivation of the tenant's enjoyment of the lease. Lord Wilberforce said:⁷¹ 'this does not approach the gravity of a frustrating event. Out of 10 years it will have lost under two years of use: there will be nearly three years left after the interruption has ceased.'

4. DEFAULT AND SELF-INDUCED FRUSTRATION

- 16.15 The party pleading frustration must not have brought the incapacitating event upon himself. The 'outside event or extraneous change of situation' must not be something which the party 'seeking to rely on it had the means and opportunity to prevent'.⁷² Bingham LJ said in *The Super Servant Two* (1990) that the concept of breach of a duty by the defendant should not be placed into a legal 'straitjacket' and that a party's fault is normally incompatible with frustration:

[T]he real question ... is whether the frustrating event relied upon is truly an outside event or extraneous change of situation or whether it is an event which the party seeking to rely on it had the means and opportunity to prevent but nevertheless caused or permitted to come about. *A fine test of legal duty is inappropriate; what is needed is a pragmatic judgment whether a party seeking to rely on an event as discharging him from a contractual promise was himself responsible for the occurrence of that event.*⁷³

More precisely, the doctrine of 'self-induced frustration' can arise where the alleged frustrating event is in fact attributable to: (1) a party's breach of contract;⁷⁴ or (2) perhaps other forms of blameworthy conduct (although this situation might be treated as turning on breach of an implied term) (see the text below for more on this category); or (3) his criminal wrongdoing;⁷⁵ or (4) his 'choice' or 'election' to prefer his own interests or those of another customer.⁷⁶

As for (2), there are *dicta* in the House of Lords decision in the *Joseph Constantine* case (1942) concerning the hypothetical *prima donna* who catches a cold through neglect of her health, but this discussion was inconclusive.⁷⁷ It is submitted that the law should recognise an implied term that a person will take reasonable steps, and avoid obvious risks, to keep open the possibility that he will be physically able to perform his contract. Breach of such an implied term will involve 'self-induced frustration' and render him liable to pay damages.

⁷¹ *Ibid.*, at 697–8.

⁷² *J Lauritzen v. Wijsmuller BV ('The Super Servant Two')* [1990] 1 Lloyd's Rep 1, 8, CA (hereafter '*The Super Servant Two*').

⁷³ *Ibid.*, at 10 (emphasis added).

⁷⁴ *Paul Wilson v. Blumenthal ('The Hannah Blumenthal')* [1983] 1 AC 854, HL; see also *The Monarch SS* case, [1949] AC 196, HL.

⁷⁵ *FC Shepherd v. Jerrom* [1987] QB 301, CA.

⁷⁶ *Maritime National Fish v. Ocean Trawlers* [1935] AC 524, PC; '*The Super Servant Two*' [1990] 1 Lloyd's Rep 1, CA.

⁷⁷ *Joseph Constantine SS Co. v. Imperial Smelting Corporation Ltd* [1942] AC 154, 166–7, 179, 195, 202, HL; see also '*The Super Servant Two*' [1990] 1 Lloyd's Rep 1, 8, CA ('fault' is inconsistent with frustration).

- 16.16 Nor can a party invoke his own default when it tactically suits him, in order to escape the conclusion that the contract has been terminated by frustration operating automatically on the relevant facts. This unsurprising proposition emerges from *FC Shepherd v. Jerrom* (1986).⁷⁸

In this case, an employee had been convicted of a crime committed out of work and sentenced to a period of Borstal training, which lasted thirty-nine weeks. He later brought a claim for unfair dismissal under the employment protection legislation (a complaint which is heard by an employment tribunal). The question was whether (1) the employer had dismissed the employee (as the latter contended) or (2) whether the contract had been terminated by operation of law, in accordance with the doctrine of frustration. The Court of Appeal concluded that it was a case of (2), and so the employee's complaint should fail *in limine*.

The curious twist, therefore, was that the employee, in order to contend for analysis (1), tactically pleaded that it was his own criminal wrongdoing which had induced the frustration: therefore, his contract had not been terminated automatically by reason of frustration; therefore, the contract had ended only as a result of his employer's decision to dismiss him. But this bold argument failed. The Court of Appeal held that it would be inappropriate for a party to plead his own self-induced frustration in this counter-intuitively self-serving fashion. Accordingly, there had been a frustration by operation of law and thus no active dismissal by the employer. There had been no 'dismissal', merely a cessation of employment, which occurred without the employer's decision.

- 16.17 *Choice precludes frustration.* '*The Super Servant Two*' (1990)⁷⁹ decides that frustration does not apply if it remained physically possible for a party to have performed his contract, but he chose not to do so, either (1) because he preferred to advance his own interests, or (2) because he had committed himself to use the available resources for a contract with another party (taking the risk of a clear, or at least potential, 'double-booking'). It is not enough, therefore, that in either of these situations the crisis has arisen from a supervening event without that party's default. However much sympathy one might have for his plight, the fact that this party has made this choice destroys any chance of frustration applying. Situation (1) is illustrated by the *Maritime National* case (1935)⁸⁰ and (2) by '*The Super Servant Two*' (1990).⁸¹ These cases will be considered in turn.

- 16.18 In the *Maritime National* case (1935) (for the facts, see 16.06 above), the Privy Council held that the defendant's allocation of the three licences to ships other than the present chartered vessel was an act of self-induced frustration.⁸² The decision is fair but is open

78 [1987] QB 301, CA; on which see M. Mustill, 'Anticipatory Breach', in *Butterworths Lectures 1989–90* (London, 1990), 3, 75–6.

79 '*The Super Servant Two*' [1990] 1 Lloyd's Rep 1, 10, CA.

80 *Maritime National Fish Ltd v. Ocean Trawlers Ltd* [1935] AC 524, PC.

81 '*The Super Servant Two*' [1990] 1 Lloyd's Rep 1, 10, CA.

82 *Maritime National Fish* case, [1935] AC 524, PC.

to two interpretations. The first is that the defendant was unable to escape liability to the claimant because his decision to use the licences for vessels other than the claimant's was his own 'free choice'. In the case itself, it could have been contended that the defendant had selfishly preferred to use the licences for his own boats, knowing that this would affect his dealings with the claimant. Alternatively, the decision might be interpreted as establishing the principle that any element of choice on the defendant's part precludes frustration, even if the defendant had at the relevant time no real freedom of decision. English law has adopted the latter and stricter approach, as the next case shows.

- 16.19 The second, and now the leading, decision on this topic is '*The Super Servant Two*' (1990).⁸³ The decision boils down to this: if Y hires out to X either vessel SS I or vessel SS II, the allocation being postponed to suit Y, supervening and excused unavailability of SS II does not also excuse Y from his duty to provide SS I, which is the back-up vessel. It is of no relevance to X that Y has double-booked SS 1, the back-up vessel, having decided to use it to make money in a contract with a different customer.

In '*The Super Servant Two*' (1990), the defendant contracted to carry the claimant's drilling rig from Japan to Rotterdam on either of his two giant barges, *The Super Servant One* or *The Super Servant Two*. After the contract's formation, the defendant decided to allocate *Two* for this job, using *One* for another job with a third party (these giant barges seem to have been commercially interchangeable, possessing the same dimensions, etc.). But, before the *Two* could be moved to work on the claimant's job, that vessel sank in the Zaire River. The terms of the contract stated that the contract could be performed by the use of either of two named vessels: the contract did not restrict performance to the vessel which, on these facts, later became unavailable through no fault of the owner. The fact that the contract could be performed using alternative vessels could work to the rig-owner's advantage (increasing the chances of a barge remaining available) and to the barge-owner's advantage (enabling him to avoid the other party's potentially problematic objection that only a single nominated vessel could be used for the job).

The Court of Appeal held that the sinking of *Two* did not exonerate the defendant. The contract with the claimant had stipulated that either *One* or *Two* would be used. The defendant could not hide behind its own commercial decision to use *One* for the parallel contract with the third party. There was no reason why the claimant should suffer as a result of the defendant's commercial deployment of his remaining vessel. That deployment had been made to suit the defendant, and he had earned extra revenue from it.

The decision is sound. There was no commercial merit in the plea of frustration on these facts. As Bingham LJ observed, the defendant's option to use *One* or *Two* had been inserted by the defendant for its commercial convenience.⁸⁴ Similarly, Dillon LJ noted

⁸³ '*The Super Servant Two*' [1990] 1 Lloyd's Rep 1, CA.

⁸⁴ *Ibid.*, at 10.

that the defendant had extracted *extra revenue* from its *One* customers before finally allocating *Two* to the contract with the claimant.⁸⁵ And so the Court of Appeal was right to conclude that the claimant was entitled to damages. The claimant was entitled to compensation for the more expensive transport arrangements incurred by him as a result of the defendant's failure to provide a barge. It would have been different if the contract had exclusively nominated *Two*⁸⁶ (assuming, of course, that its subsequent sinking was not attributable to the defendant's default). That would have sent the clear message: 'everything depends on the physical availability of *Two*; if it sinks etc., without my fault, you cannot sue me for non-supply.'

A final aspect of this case is that the contract contained a *force majeure* clause (16.09) which literally would be effective to exclude the defendant's liability arising from the sinking of *Two*. But the Court of Appeal held that this clause would not exonerate the defendant if there had been negligence on its part. Since the litigation was being conducted at this stage on preliminary points, the eventual result is not reported.

- 16.20** *The conundrum of short supply and too many customers.* Suppose that a Lincolnshire pea farmer, D, agrees to supply in the 2010 season 100 tonnes to each of X, Y and Z at a specified rate of payment. This is a reasonable contract since last year D achieved a yield of 500 tonnes in all. But, because of natural events outside his control, the 2010 yield is only 100 tonnes. What can D do? The following discussion assumes that D has failed to contract on the basis that his commitment to supply is 'subject to availability, including adverse growing conditions'. English law is clear: none of the contracts is frustrated; and so Y and Z have good claims for breach of contract against D if he delivers the 100 tonnes to X. This approach is supported by '*The Super Servant Two*' decision (see 16.23 above). Some might regard this as harsh. The better view, however, is that the English rule is commercially realistic and the result is clear. Of course, different approaches might have been adopted: to allow D a defence if his decision to supply X was based on the fact that D's contract with X was concluded before the other contracts (first come, first served) or if he split his 100 tonnes equally between X, Y and Z, regardless of the contract date.⁸⁷

Of course, on different facts, if a farmer without fault finds that he has insufficient goods to supply a single buyer, and it was apparent that the farmer was agreeing to supply peas produced from his land, the contract will be partially frustrated to the extent of the shortfall: X agrees to supply 100 tonnes of peas to Y. There are no other buyers. Due to unprecedented hailstorms, X's yield is only 50 tonnes. X is excused from failure to supply more than 50 tonnes.

⁸⁵ *Ibid.*, at 13 col. 2.

⁸⁶ *Ibid.*, at 9 col. 2, *per* Bingham LJ.

⁸⁷ G. H. Treitel, *Frustration and Force Majeure* (2nd edn, London, 2004), 5-015 ff; for this approach in the USA, see Uniform Commercial Code, section 2-615; cases adopting such an approach are distinguished in '*The Super Servant Two*' [1990] 1 Lloyd's Rep 1, 9 col. 1, as applicable to construction of *force majeure* clauses; Dillon LJ in particular [1990] 1 Lloyd's Rep 1, 13-14, rejected a 'reasonableness' approach; on these cases, see G. H. Treitel, *Frustration and Force Majeure* (2nd edn, London, 2004), 5-020 ff.

5. THE AFTERMATH OF FRUSTRATION⁸⁸

16.21 Frustration ‘brings the contract to an end forthwith, without more and automatically’ (that is, without any need for the parties to be aware that it has occurred).⁸⁹ It releases the parties from their unperformed obligations. For most types of contract, the Law Reform (Frustrated Contracts) Act 1943 has ameliorated the following three common law consequences of frustration:

- (1) At common law, money paid before the contract is frustrated can be recovered only if there is a total failure of consideration. In the *Fibrosa* case (1943),⁹⁰ the House of Lords reversed the Court of Appeal’s entirely fallacious decision in *Chandler v. Webster* (1904),⁹¹ which had wrongly held that there can be no total failure of consideration unless a contract is rescinded *ab initio*. Instead, as the House of Lords clarified, it is enough that there has been a complete absence of performance by the payee under the contract which has now been terminated for frustration.
- (2) At common law, accrued obligations to pay remained enforceable.
- (3) At common law, there was no scope to award recompense for partially completed work (this is because of the doctrine of entire obligations: payment is owed for contractual performance only if that performance, or a severable part of it, is completed or substantially performed before the contract’s frustration; generally on the common law doctrine of entire obligations and substantial performance, see 17.51).

16.22 In *BP Exploration Co. (Libya) Ltd v. Hunt (No. 2)* (1979), Robert Goff J commented as follows on the effect of sections 1(2) and (3) of the Law Reform (Frustrated Contracts) Act 1943:⁹²

The [Act] is not designed to do certain things: (i) It is not designed to apportion the loss between the parties ... (ii) It is not concerned to put the parties in the position in which they would have been if the contract had been performed. (iii) It is not concerned to restore the parties to the position they were in before the contract was made.

16.23 Section 1(2) of the 1943 Act states (the provision vies with section 1(3), see 16.25 below, for being the most convoluted sentence on the statute book):

All sums paid or payable to any party in pursuance of the contract before the time when the parties were so discharged (in this Act referred to as ‘the time of discharge’)

⁸⁸ Treitel, *ibid.*; E. McKendrick (ed.), *Force Majeure and Frustration of Contract* (2nd edn, London, 1995); R. Goff and G. H. Jones, *The Law of Restitution* (7th edn, London, 2007), 20–61 ff; S. Hedley and M. Halliwell (eds.), *The Law of Restitution* (London, 2002), chapter 20; E. McKendrick, ‘Frustration, Restitution and Loss Adjustment’, in A. Burrows (ed.), *Essays on Restitution* (Oxford, 1991), 147; G. L. Williams, *Law Reform (Frustrated Contracts) Act 1943* (1944).

⁸⁹ *Hirji Mulji v. Cheong Yue Steamship Co. Ltd* [1926] AC 497, 505, PC, *per* Lord Sumner.

⁹⁰ *Fibrosa Spolka Akcyjna v. Fairbairn Lawson Combe Barbour Ltd* [1943] AC 32, 45–8, HL.

⁹¹ [1904] 1 KB 493, 499–501, CA, *per* Lord Collins MR.

⁹² The main discussion by Robert Goff J is at [1979] 1 WLR 783, 799; subsidiary aspects are examined in successive appeals, [1981] 1 WLR 232, CA; [1982] 2 AC 352, HL.

shall, in the case of sums so paid, be recoverable from him as money received by him for the use of the party by whom the sums were paid, and, in the case of sums so payable, cease to be so payable: Provided that, if the party to whom the sums were so paid or payable incurred expenses before the time of discharge in, or for the purpose of, the performance of the contract, the court may, if it considers it just to do so having regard to all the circumstances of the case, allow him to retain or, as the case may be, recover the whole or any part of the sums so paid or payable, not being an amount in excess of the expenses so incurred.

The effect of section 1(2) is that a party can reclaim money paid before the frustrating event, even if there has been some partial performance by the recipient. This reverses the *Fibrosa* case (1943) in this context.⁹³ But this refund is subject to the recipient's counter-claim for an allowance for his expenditure: see the second part of section 1(2), after the words 'Provided that ...' above. The allowance referred to therein is at the court's discretion (16.24).

Another aspect of section 1(2) is that it reverses the common law by *prima facie* cancelling an outstanding liability to pay if this duty has arisen (liability has 'accrued') before the contract was frustrated. But this provisional cancellation can be reversed, in whole or in part, if, in exercise of the court's discretion (16.24), it is decided that the intended payee should be paid such unpaid sums to cover the payee's expenditure.

- 16.24 Thus, under section 1(2) of the 1943 Act, the court receives a twofold discretion: to order repayment; and to reverse cancellation of debts already accrued. In *Gamerco SA v. ICM/Fair Warning (Agency) Ltd* (1995), Garland J held that the court has a free hand when exercising these discretions.⁹⁴ He rejected two rigid approaches: to split the payee's reliance on an equal basis between him and the payor; or to allow the payee always to retain the money to the extent of his reliance.

In the *Gamerco* case (1995), the claimant company had hired the defendant rock band to perform at a concert in a Madrid stadium. The contract was subject to English law. After the contract's formation, the Spanish authorities condemned the proposed venue as unsafe. This prohibition was, therefore, a supervening event. As a result, the contract had been frustrated. The claimant had made a large prepayment to the band.

The question was whether the judge should exercise his discretion to allow them to retain some or even all of that payment. The defendant/payee has the onus of establishing that there should be some 'discretionary retention'.⁹⁵ But, in this case, the defendant had not adduced clear evidence of its expenditure in preparation for the concert.⁹⁶ The judge rejected the view

⁹³ [1943] AC 32, HL.

⁹⁴ [1995] 1 WLR 1226.

⁹⁵ *Ibid.*, at 1235G.

⁹⁶ *Ibid.*, at 1237F.

that section 1(2) should be applied to give the payee 'total retention' of sums paid or payable, or that the losses suffered by both parties should be cumulated and then split equally, by adjustment of the award under this sub-section.⁹⁷

On balance, the judge decided that the claimant deserved to recover the whole prepayment. Its own wasted expenditure certainly exceeded the amount of that recovery. The case identifies the open nature of this discretion under section 1(2), and the practical importance of the payee bearing the burden of proof when seeking to establish the need for a favourable exercise of this discretion.

16.25 What of performance other than by payment of money (use of goods or performance of services)? Section 1(3) of the 1943 Act provides:

Where any party to the contract has, by reason of anything done by any other party thereto in, or for the purpose of, the performance of the contract, obtained a valuable benefit (other than a payment of money to which the last foregoing subsection applies) before the time of discharge, there shall be recoverable from him by the said other party such sum (if any), not exceeding the value of the said benefit to the party obtaining it, as the court considers just, having regard to all the circumstances of the case and, in particular—

- (a) the amount of any expenses incurred before the time of discharge by the benefited party in, or for the purpose of, the performance of the contract, including any sums paid or payable by him to any other party in pursuance of the contract and retained or recoverable by that party under the last foregoing subsection, and
- (b) the effect, in relation to the said benefit, of the circumstances giving rise to the frustration of the contract.

The effect of section 1(3), therefore, is that the court, at its discretion, can award a 'just sum' to the party whose *work or provision of goods* has conferred, before the date of discharge (automatic discharge by frustration) a 'valuable benefit' (that is, a benefit other than payment of money, a matter falling within section 1(2); see above); and he might be awarded an amount which the court considers just in respect of that benefit, taking into account the impact of the frustrating event upon the relevant benefit.

16.26 The only reported English case on section 1(3) of the 1943 Act is *BP Exploration Co. (Libya) Ltd v. Hunt (No. 2)* (1979).⁹⁸

The claimant, British Petroleum, had entered into a complicated joint venture with the defendant, Hunt. The parties had agreed to develop and exploit an oil field in Libya. Hunt

⁹⁷ *Ibid.*, at 1236–7.

⁹⁸ The main discussion by Robert Goff J is at [1979] 1 WLR 783; subsidiary aspects are examined in successive appeals, [1981] 1 WLR 232, CA; [1982] 2 AC 352, HL.

owned the oil concession. The terms of this contract gave BP a right to 'reimbursement oil'. Once reimbursed for its expenditure in developing the oil field, the oil revenue would be divided equally between the two parties. BP expended large sums on the project. As a result, the parties succeeded in extracting oil. The contract had operated successfully for almost five years, when the Libyan government decided to expropriate the oil field.

Robert Goff J held that, in principle, the valuable benefit obtained by Hunt on these facts was not the oil but the enhancement of the value of the oil rights. So the judge assessed the benefit by reference to the amount of oil received by Hunt and the amount of the Libyan government's compensation for the expropriation. The total was approximately US\$85m. He then awarded a 'just sum' of approximately US\$11m, which took account of: (1) the fact that the field had been expropriated; (2) the parties' pre-existing receipts under the contract; and (3) Hunt's recovery of modest compensation from the Libyan government.

- 16.27 Perhaps a more illuminating approach to section 1(3) is to take the following hypothetical case. Suppose A agrees with B to build a factory for £2m. Halfway through the job, the factory is destroyed in a fire caused by vandals. At that point, A had spent £1.25m. No money was yet owed by B to A. Goff J suggested in the following *dictum* in *BP v. Hunt* (No. 2) that the valuable benefit under section 1(3) in this context would be the scrap value of A's ruined work:⁹⁹

[T]he benefit should in an appropriate case be identified as the end product of the services ... Let me take the example of a building contract. Suppose that a contract for work on a building is frustrated by a fire which destroys the building and which, therefore, also destroys a substantial amount of work already done by the plaintiff ... It is quite plain that, in section 1(3)(b), the word 'benefit' is intended to refer, in the example I have given, to the actual improvement to the building, because that is what will be affected by the frustrating event; the subsection therefore contemplates that, in such a case, the benefit is the end product of the plaintiff's services, not the services themselves.

Treitel convincingly takes issue with this analysis.¹⁰⁰ He notes that section 1(3) requires the court to identify a 'valuable benefit' obtained 'before' the contract's termination. The relevant 'valuable benefit', therefore, would be the value of the building before the conflagration. Then, Treitel observes, the structure of section 1(3) requires the court to assess a 'just sum'; and in making this assessment it must take into account all the factors, including, as directed by section 1(3)(b), the impact on the valuable benefit of the events giving rise to the frustration. On the present imaginary¹⁰¹ facts, the fire destroyed the building. On this basis, it seems likely that the court would fix the valuable benefit at

⁹⁹ [1979] 1 WLR 783, 801–2.

¹⁰⁰ *Treitel* (12th edn, London, 2007), 19–103 (discussing the facts of *Appleby v. Myers* (1867) LR 2 CP 651).

¹⁰¹ The nineteenth-century case, *Appleby v. Myers* (1867) LR 2 CP 651, involved very similar facts (a factory consumed by fire, causing destruction of, among other things, machinery installed by one of the parties); although, of course, this case antedated the 1943 Act.

either £1m or £1.25m. It might then split this loss between A and B. But the court has a complete discretion whether to give A full protection, zero protection or a partial award. The court cannot award more than the valuable benefit.

This discussion of the building which burns down concerns a situation where Goff J's analysis requires identification of an 'end product', a term not in fact used in section 1(3). However, Goff J added that the end-product analysis will not apply to services consisting of the surveying of land or the transport of goods:¹⁰² '[I]n some cases the services will have no end product; for example, where the services consist of doing such work as surveying, or transporting goods. In each case, it is necessary to ask the question: what benefit has the defendant obtained by reason of the plaintiff's contractual performance?'

16.28 Section 1(5) of the 1943 Act provides that, if an express term of the contract *required* B (or A) to insure against a risk, that term must be taken into account for the purpose of determining whether any sum should be recovered or retained under section 1(2) and section 1(3). So, for example, it would be relevant if a builder were required under the contract to insure his building work against destruction or damage before the building is completed. But, if either A or B had in fact decided to take out insurance, *even though he had not been expressly bound to do so under the A/B contract*, the court *cannot* take the fact of insurance into account. The rationale of this distinction is that a contractual allocation of risk can be inferred (and then taken into account under the Act) only if one party was contractually obliged to take out insurance.

16.29 *Summary of sub-sections 1(2) and 1(3).*

(1) Section 1(2) of the 1943 Act permits the court or arbitrator to engage in *qualified loss adjustment*. The device used is that of a 'kitty' consisting of sums paid or payable before the time of contractual termination:

- (a) *prima facie* that sum is repayable or the sum payable need not be paid; but
- (b) this is qualified by the court's discretion to allow the 'kitty' holder to keep or recover in respect of his expenses.

As for (b), *Gamerco SA v. ICM/Fair Warning (Agency) Ltd* (1995)¹⁰³ emphasises the absence of rules or even a presumption governing how that kitty is to be distributed under the Act.

- (2) Section 1(3) can be rationalised as the award of a *restitutionary* valuation of the benefit of non-monetary contractual performance, subject to discretionary loss adjustment (award of a just sum not to exceed the valuable benefit received).
- (3) Although section 1(2) can be loosely explained as reflecting the commercial implication that money paid or payable is available to protect the payee, section 1(3) rests on no such parallel implication. The truth is, therefore, that section 1(3) is a *hybrid*

¹⁰² [1979] 1 WLR 783, 801–2.

¹⁰³ [1995] 1 WLR 1226, Garland J.

device, allowing qualified restitution for non-monetary benefits. As McKendrick has aptly said:¹⁰⁴

[T]he 1943 Act does not empower the court to apportion losses between parties ... While the Act does confer a discretion upon the court [under section 1(2) and (3)], it is not a discretion that relates explicitly to the apportionment of losses. In all cases the court must first identify the benefit which the defendant has obtained at the expense of the claimant. The discretion given to the court relates only to the proportion of that benefit which is recoverable by the claimant. It is a discretion exercisable within a framework which seeks to prevent the unjust enrichment of one party at the expense of the other.

6. TERMINATION OF CONTRACTS OF INDEFINITE DURATION¹⁰⁵

- 16.30 Long-term contracts, unless of fixed duration, are subject to an implied term enabling one party to give reasonable notice to the other that the contract will be terminated.

For example, in *Staffordshire Area Health Authority v. South Staffordshire Waterworks Co.* (1978), a majority of the Court of Appeal held that a 1929 agreement to supply 5,000 gallons of water a day free of charge, thereafter at seven old pence per 1,000 gallons 'at all times hereafter', was neither a perpetual contract nor (as was evident) a contract of fixed duration. Since the contract was of indefinite duration, the Court of Appeal held that it was terminable by the giving of reasonable notice.¹⁰⁶ The water company was prepared to continue the supply, charging, for daily usage in excess of 5,000 gallons, the 1970s price for commercial supply (see further 17.04).

If the contract is of a *fixed duration*, there will be no implied term that a party can terminate it by giving reasonable notice, as *Jani-King (GB) Ltd v. Pula Enterprises Ltd* (2007) shows.¹⁰⁷ A contractual provision literally couched as conferring on a party a 'perpetual' entitlement must be construed against the relevant commercial context. On the facts of *BMS Computer Solutions Ltd v. AB Agri Ltd* (2010),¹⁰⁸ Sales J, in the Chancery Division, held that the word 'perpetual' did not confer an everlasting entitlement under a commercial licence, but merely an entitlement of no fixed duration.¹⁰⁹ Accordingly, the licence could be validly terminated under various provisions within the document, including

104 E. McKendrick, *Contract Law: Text, Cases and Materials* (4th edn, Oxford, 2010), 744.

105 McKendrick, 'The Regulation of Long-Term Contracts in English Law', in J. Beatson and D. Friedmann (eds.), *Good Faith and Fault in Contract Law* (Oxford, 1995), 305.

106 [1978] 1 WLR 1387, CA, *per* Goff and Cumming-Bruce LJ; at *ibid.*, 1397–8, Lord Denning MR, in a minority opinion, reached the same conclusion by the heterodox route of finding frustration to be satisfied by inflation; T. A. Downes, (1985) 101 LQR 98, 104–8.

107 [2007] EWHC 2433 (QBD); [2008] 1 Lloyd's Rep 305, at [60] to [66], *per* Coulson J; also, on this case, see 13.13 and 13.23.

108 [2010] EWHC 464 (Ch).

109 See his cogent articulation of supporting reasons, *ibid.*, at [18].

unilateral termination upon giving a specified period of notice. Finally, as decided in *ServicePower Asia Pacific Pty Ltd v. ServicePower Business Solutions Ltd* (2009), the court will not give effect to an implied termination clause if an express term already covers that topic.¹¹⁰

7. POST-FORMATION HARDSHIP: EXCEPTIONAL DENIAL OF SPECIFIC PERFORMANCE

- 16.31 The court can withhold specific performance (on this *equitable* remedy, see 18.14) if events subsequent to the contract's formation have rendered it unjust to compel the relevant party to perform. Those events must render such an order excessively harsh. The relief is confined to the remedy of specific performance: the contract *is not frustrated*. And so the party failing to perform will be liable to pay compensation at common law for failure to honour his subsisting obligations. Therefore, this is a ground of relief recognised exceptionally, and only within equity (on the common law/equity distinction, see 1.25). A rather isolated example is *Patel v. Ali* (1984), where Goulding J refused to order specific performance against the vendor of domestic premises because, since the contract's formation, she had lost a leg *and* this physical disability now made it necessary for her to remain close to people capable of assisting her.¹¹¹ The decision did not involve frustration of the contract, merely the *equitable discretion whether to withhold the remedy of specific performance*. The common law action for damages (18.23) remained available. And Goulding J ordered £10,000 to be paid into court by the defendant as security to support the claimant's right to compensation. The case was remitted to another judge for an 'inquiry' into (assessment of) damages. The courts should be slow to broaden this category.

¹¹⁰ [2009] EWHC 179 (Ch); [2010] 1 All ER (Comm) 238, at [25] ff (William Trower QC).

¹¹¹ [1984] Ch 283, Goulding J.

Chapter contents

1. Introduction *para. 17.01*
2. Anticipatory breach *para. 17.11*
3. Renunciation at the date of performance *para. 17.16*
4. Terminating for breach of condition or other serious breach *para. 17.18*
5. Relief against forfeiture of proprietary or possessory interests *para. 17.39*
6. The process of termination for breach *para. 17.41*
7. Termination for breach and rescission for misrepresentation etc. contrasted *para. 17.48*
8. The entire obligation rule *para. 17.51*

17

Breach and performance

1. INTRODUCTION¹

17.01 Summary of main points

- (1) Breach involves an unexcused failure to perform a positive contractual obligation (whether the obligation is contained in an express or implied term), or doing something which one has promised not to do (breach of a 'negative undertaking').
- (2) Breach arises if the infringement at (1) occurs without lawful excuse, that is, unless excused under general law (the doctrine of frustration: see 16.01 ff), or unless excused by a particular clause, for example, a *force majeure* clause (stipulating that a party will be released from his obligation by reason of freak and excusable supervening events: see 16.09).²
- (3) Breach exposes the guilty party to a claim for damages, or debt, or specific performance, or an injunction, or at least a declaration that breach has occurred (for a survey of these remedies, see 18.02).

1 J. Birds, R. Bradgate and C. Villiers, *Termination of Contracts* (London, 1995), chapters 1, 2 and 10; J. Carter, *Breach of Contract* (2nd edn, Sydney, 1991); M. Mustill, 'Anticipatory Breach', *Butterworths Lectures 1989–90* (London, 1990); J. E. Stannard, *Delay in the Performance of Contractual Obligations* (Oxford, 2007). For comparative and foreign law, see: G. H. Jones (with P. Schlechtriem), 'Breach of Contract', in *International Encyclopaedia of Comparative Law*, vol. VII, *Contracts in General* (Tübingen, 1999), chapter 15 (Anglo-American, Commonwealth and civilian laws); G. H. Treitel, *Remedies for Breach of Contract: A Comparative Account* (Oxford, 1988); for US law, see E. A. Farnsworth, *Contracts* (4th edn, New York, 2004), chapter 8.

2 E. McKendrick (ed.), *Force Majeure and Frustration of Contract* (2nd edn, London, 1995), especially at 34; E. McKendrick, 'The Regulation of Long-Term Contracts in English Law', in J. Beatson and D. Friedmann (eds.), *Good Faith and Fault in Contract Law* (Oxford, 1995), 305, 323 ff; *Chitty on Contracts* (30th edn, London, 2008), 14–137 ff; E. McKendrick, *Contract Law* (8th edn, London, 2009), 14.9.

- (4) The main forms of breach are:
 - (a) *Anticipatory breach*. This occurs before performance is required. This form of breach was recognised in *Hochster v. De La Tour* (1853) (17.12),³ which established that the innocent party need not wait to see whether there might be a change of mind by the other party; instead, the innocent party can 'elect' to end the contract straightaway and sue for compensation.
 - (b) *Renunciation on the day of performance*. At the time of the promised performance, a party might announce that he is unwilling to perform the contract, a case of renunciation.
 - (c) *Breach by non-feasance or misfeasance*. At the time of the promised performance, he might fail to perform at all (a case of total non-performance), or his performance might not comply with the contract; or breach might involve the commission of an act in contravention of a 'negative undertaking', that is, an obligation prohibiting that act, for example, by working for a rival company.
 - (d) *Dilatory performance*. He might eventually perform, but only after delay.
- (5) Every breach entitles the innocent party to recover at least 'nominal damages' (a token sum signifying the fact that there has been a technical legal wrong, for example, sums of £5 or £10).⁴
- (6) The innocent party is entitled to terminate a contract for breach if (17.18):
 - (a) the other party has shown a clear unwillingness to satisfy his contract ('renunciation', sometimes known as 'repudiatory breach'); or
 - (b) performance has been rendered impossible by the default of the guilty party; or
 - (c) there has been a breach of an important term (a 'condition') or of another term which can give rise to termination, depending on the seriousness of the breach (an 'innominate term').
- (7) A 'condition' (that is, condition in the sense of a promissory obligation: see 17.19) will arise when statute so provides, or if the relevant obligation is expressed to be a 'condition' (see, however, (8) below) or it is subject to a clause entitling the innocent party to terminate the contract for failure to satisfy the obligation, or if the court construes a neutral term as a condition.
- (8) Express use of the word 'condition' is not decisive because, exceptionally, the courts are prepared to 'construe away' this word as not intended to bear the technical meaning just mentioned (see *Schuler v. Wickman* (1974)); there is also a qualification in section 15A of the Sale of Goods Act 1979.

3 (1853) 2 E & B 678; 22 LJ (QB) 455; P. Mitchell, in C. Mitchell and P. Mitchell (eds.), *Landmark Cases in the Law of Contract* (Oxford, 2008), 135.

4 *McGregor on Damages* (18th edn, London, 2009), chapter 10.

- (9) Faced by the other party's repudiation (anticipatory breach, or renunciation at the time of due performance, or other breach which justifies termination), the innocent party has a choice (17.15, 17.41, 18.05): he can accept the repudiation and thus terminate the contract and sue for damages, or he can affirm the contract and sue for damages.⁵ This is known as 'the right to elect'.
- (10) Termination for breach operates to end the contract from that point in time, but only prospectively; it does not annihilate the contract retrospectively (17.48). The innocent party retains the right to sue in respect of preceding breaches. 'Rescission' is now confined to the quite distinct process of setting aside retrospectively a contract which is vitiated by reason of misrepresentation, or the other grounds mentioned above, and restoring the parties to the original position as though the contract never existed.
- (11) The question of breach is technically distinct from the right to refuse performance if the other side has failed to complete performance of an obligation, where the parties' obligations are 'dependent' (see 17.05 below; in detail, at 17.51 below).

Anticipatory breach

M. Mustill, *Anticipatory Breach: Butterworths Lectures 1989–90* (London, 1990)

Repudiation

E. Peel, 'Misinterpretation of Contractual Rights and Repudiation' [1996] LMCLQ 309

Promissory terms

'Condition' not necessarily a 'condition': case notes on the Schuler case

J. H. Baker, [1973] CLJ 196

R. Brownsword, (1974) 37 MLR 104

F. A. Mann, (1973) 89 LQR 464

Terms aimed at permitting innocent party to terminate

S. Whittaker, 'Termination Clauses', in A. Burrows and E. Peel (eds.), *Contract Terms* (Oxford, 2007), chapter 13 (at 273–83 on the *Rice* case) (Whittaker's chapter contains a valuable discussion of many related decisions concerning 'material breach' and similar contract drafting)

⁵ *Fercometal SARL v. Mediterranean Shipping Co. SA ('The Simona')* [1989] AC 788, HL; *Vitol SA v. Norelf Ltd ('The Santa Clara')* [1996] AC 800, HL.

Innominate terms

A. Weir, [1976] CLJ 33 on '*The Hansa Nord*' (1976), applying the *Hongkong Fir* case (1962)

History of warranties and conditions

D. J. Ibbetson, *A Historical Introduction to the Law of Obligations* (Oxford, 1999), 83–7

Entire obligation rule

B. McFarlane and R. Stevens, 'In Defence of *Sumpter v. Hedges*' (2002) 118 LQR 569, especially at 572–86 and 594 ff

17.02 *Main forms of breach.* Breach can occur in the following situations:

Breach occurring before the date for performance

- (1) *Explicit anticipatory breach.* Here, before performance is required, a party makes clear that he does not intend to perform. Such 'anticipatory breach' was not recognised until *Hochster v. De La Tour* (1853). This decision, and later cases, established that the innocent party need not wait to see whether there might be a change of mind; instead, the innocent party can 'elect' to end the contract straightaway and sue for compensation.⁶
- (2) *Inferred anticipatory breach by self-disablement: apparent that eventual performance has been rendered impossible.* Before the performance is due, it might become apparent that B has prevented the contract from being performed, and that A can safely infer that B will be unable to perform.

Breach occurring at or after the date for performance

- (3) *Repudiation on day of performance.* At the time of the promised performance, the guilty party might announce that he is unwilling to perform the contract, a case of repudiatory breach (although use of the word 'repudiatory' in this non-anticipatory context has been deprecated).⁷
- (4) *Inaction or 'no-show' on day of performance.* At the time of the promised performance, he might remain silent and fail to perform at all, a case of total non-performance (breach compounded by insolent muteness); or he might simply fail to communicate or appear.
- (5) *Bad performance.* He might act, but badly, by delivering goods or providing services which are defective in quality, or (especially in the case of goods) do not correspond to the amount ordered.
- (6) *Dilatory performance.* He might perform but only after delay, or his performance might start promptly but be delayed in completion.

⁶ (1853) 2 E & B 678 (discussed at 17.12).

⁷ '*The Hansa Nord*' [1976] QB 44, 59D, CA, *per* Lord Denning MR.

- (7) *Breach of promise not to act.* Breach might involve the commission of an act in contravention of a 'negative undertaking', that is, in breach of an obligation prohibiting that act, for example by working for a rival company.

17.03 '*Repudiatory breach*'. The expression 'repudiatory breach' can denote various situations: (1) an anticipatory breach by renunciation; or (2) renunciation at the time of expected performance; or (3) substantial breach justifying termination (breach of a condition or serious breach of an intermediate term); or (4) a pattern of breach justifying the inference that the guilty party no longer intends to comply substantially with the contract (see 17.38 concerning *Rice v. Great Yarmouth Borough Council* (2000)).⁸ It is suggested that 'renunciation' is a clearer way of expressing the forms of breach in (1) and (2), and that the phrase 'repudiatory breach' might be usefully confined to categories (3) and (4).

17.04 *Termination rights.* There are three possible types of termination right:

- (1) an express right to cancel without breach;
- (2) an express right to terminate for breach; and
- (3) an implied right to cancel.⁹

As for clauses of type (1), namely, express rights to cancel without breach, a contract might expressly permit a party to terminate a contract in specified circumstances, even in the absence of a common law right to terminate for breach (that is, in the absence of either renunciation or of breach of a condition, or serious breach of an intermediate term). Where this occurs, the party who terminates might be entitled to obtain damages in respect of past breaches, but he will not be able to obtain damages for loss of the remaining period of the contract *unless the facts disclose that there has been a repudiatory breach in respect of which the innocent party has terminated the contract*¹⁰ (as the Court of Appeal explained in the *Lombard* case (1987), there had been no such repudiatory breach on the facts of the *Financings* case (1963)).¹¹

As for clauses of type (2), namely, express rights to terminate for breach, the Court of Appeal in *Stocznia Gdynia SA v. Gearbulk Holdings Ltd* (2009) held that it is possible for an innocent party to exercise simultaneously an express power *to terminate for breach* and the common law right to terminate a contract because of the other party's repudiatory breach (Moore-Bick LJ giving the court's sole reasoned judgment).¹² Furthermore, in

⁸ *The Times*, 26 July 2000; (2001) 3 LGLR 4, CA, at [38].

⁹ S. Whittaker, 'Termination Clauses', in A. Burrows and E. Peel (eds.), *Contract Terms* (Oxford, 2007), chapter 13.

¹⁰ *Financings Ltd v. Baldock* [1963] 2 QB 104, 110–11, 121, CA; Nicholls LJ in *Lombard North Central plc v. Butterworth* [1987] QB 527, 541–3, 546, CA; noted by G. H. Treitel, [1987] LMCLQ 143; W. Bojczuk, [1987] JBL 353; B. Opeskin, (1990) 106 LQR 293; E. McKendrick, *Contract Law: Text, Cases and Materials* (4th edn, Oxford, 2010), 772 ff.

¹¹ Nicholls LJ in the *Lombard* case, [1987] QB 527, 541–2, noting Diplock LJ in the *Financings* case, [1963] 2 QB 104, 121, CA.

¹² [2009] EWCA Civ 75; [2010] QB 27 (noted by E. Peel, (2009) 125 LQR 378–84).

the same case, it was held that an express and guaranteed right to recover prepayments can co-exist with the background common law right to terminate the contract by reason of repudiatory breach.

The *Stocznia* case (2009) concerned contracts for the construction and sale of three ships. The seller failed to supply in time, and the buyer terminated all three contracts for repudiatory breach. The buyer exercised its express right to recover, under a guarantee facility, its prepayments (see further below). But the parties went to arbitration on the disputed issue of whether this transaction's clauses, providing both for termination (for serious breach) and repayment, had the effect of precluding a general common law claim for loss of bargain consequent upon termination for repudiatory breach. The seller contended that the contract's termination machinery (for breach) was the exclusive mode of terminating for breach; or, if this express machinery were an alternative mode of termination, available alongside common law termination principles, that the buyer had elected to invoke the express machinery alone, and so had lost any chance to obtain general common law compensation for loss of bargain.

The Court of Appeal upheld the buyer's contentions. It held that this innocent party's decision to invoke the express right to guaranteed repayment of purchase instalments was not incompatible with a co-existing common law right to loss of bargain damages consequent on his termination of the contract for repudiatory breach. The Court of Appeal's decision upheld the award in favour of the buyer by a sole arbitrator, Sir Brian Neill, and the Court of Appeal's decision rejected Burton J's Commercial Court decision, on appeal, in favour of the seller.

In the Court of Appeal, Moore-Bick LJ explained the conclusion that the express right to terminate for serious default co-existed with a common law right to terminate for a repudiatory breach:¹³

[The parties had] agreed that there comes a point at which the delay or deficiency is so serious that it should entitle [the buyer] to terminate the contract ... [T]he right to terminate the contract cannot sensibly be understood as anything other than embodying the parties' agreement that the buyer has the right to treat the contract as repudiated, with ... the usual consequences ... In my view it is wrong to treat the right to terminate in accordance with the terms of the contract as different in substance from the right to treat the contract as discharged by reason of repudiation at common law. In those cases where the contract gives a right of termination they are in effect one and the same.

The court is unlikely to be satisfied that a party to a contract has abandoned valuable rights arising by operation of law unless the terms of the contract make it sufficiently clear that that was intended. The more valuable the right, the clearer the language will need to be.

Moore-Bick LJ explained that the buyer had become entitled to recover the prepayments in restitution under the principle of total failure of consideration (18.53), once the

13 *Ibid.*, at [20] and [23] (and distinguishing at [19] *Lockland Builders Ltd v. Rickwood* (1995) 77 BLR 42, CA, where the express termination for breach clause had been construed as excluding the common law right to terminate for a repudiatory breach).

contract of sale had been terminated before any delivery of the ships. The express guaranteed right to repayment was merely a specially protected consensual version of that right. And so the buyer's invocation of this guaranteed repayment did not preclude general compensatory rights for loss of bargain (namely, for the difference between the contract price and the market value of the ship at the relevant date). This can be explained, applying orthodox analysis of termination for breach, as follows. The innocent party's decision to end the contract by reason of the seller's repudiatory failure to build these ships on time involved: (a) termination of the contract's primary obligations (the duty to perform on both sides the contract's main set of obligations); (b) survival of various ancillary provisions, such as exclusion clauses, arbitration clauses and – on these facts – an express right to repayment of a prepayment; (c) the innocent party's enjoyment of a right to seek compensatory damages, including for 'loss of bargain'. The cause of action underpinning (c) is, of course, the innocent party's decision to terminate the contract by reason of the other party's repudiatory breach (or, on other facts, breach of a condition, or a very serious breach of an innominate term). On these points, Moore-Bick LJ said:¹⁴

[T]he commercial context as well as the terms of the contract make it clear that the obligation to repay instalments of the price was intended to survive the termination of the contract, whether that occurred by reason of the exercise by [the buyer] of a right to terminate expressed in the contract itself or by its acceptance of a repudiatory breach on the part of the yard, each of which had the same consequences in law.

On discharge of a contract of this kind a buyer who has paid the whole or part of the price in advance is entitled, in the absence of any agreement to the contrary, to recover what he has paid by reason of a total failure of consideration. He therefore has a right to recover in restitution any payments he has made in respect of the price, a right which is quite distinct from any right he may have (if he is the injured party) to recover damages for the loss of his bargain ... There is no inherent inconsistency ... in recovering instalments of the price under [the guaranteed repayment clause] and recovering damages for loss of bargain at common law ...

Taking into account the contract as a whole I am left in no doubt that the parties intended [the guaranteed repayment clause] to provide a remedy additional to those that would ordinarily be available to [the buyer] on termination of the contract.'

As for clauses of type (3), namely, implied cancellation rights, in long-term contracts the courts will find an *implied term* that either party can terminate the contract, without breach of contract, by giving the other reasonable notice.

¹⁴ [2009] EWCA Civ 75; [2010] QB 27, at [26] to [42] (explaining away, especially at [35], the apparently contradictory analysis in *United Dominions Trust (Commercial) Ltd v. Ennis* [1968] 1 QB 54, CA).

An example is *Staffordshire Area Health Authority v. South Staffordshire Waterworks Co.* (1978).¹⁵ This case concerned a hospital's water supply, the rate for which had been fixed since 1929 as follows: the company would 'at all times hereafter' supply to the hospital 5,000 gallons per day free of cost; the hospital would 'at all times hereafter' be at liberty to take from the mains any further quantity needed at a rate of seven old pence for each 1,000 gallons so supplied. By 1978, the date of the appeal, it had ceased to be economic for the water company to supply at the 1929 rate. The Court of Appeal held that the water company was entitled to terminate on giving reasonable notice. This was the majority approach of Goff and Cumming-Bruce LJ, the latter explaining:¹⁶ '[T]he words "at all times hereafter" mean that the obligations granted and accepted by the agreement were only intended to persist during the continuance of the agreement; and the agreement, in my view, was determinable on reasonable notice at any time.' As for future supply, the Court of Appeal contemplated that the parties would reach a compromise on the question of the new price for supply.

The third judge, Lord Denning MR, effectively agreed with the majority's reasoning, but also attempted to fashion a novel theory permitting release from contracts which have become economically very disadvantageous because of inflation. But his theory was radical, and was not accepted by the other judges in the case.

17.05 *Unfulfilled dependent obligations: right to withhold performance.* As we shall see (17.51), the doctrine of 'entire obligations' is to be distinguished from the question of breach, although these concepts can often overlap. Thus, if B's obligation is dependent on A's performance but, *for whatever reason*, A fails to achieve 'substantial performance' (on that concept 17.53) of that obligation, B is entitled to withhold performance. Normally, B's capacity to withhold performance will take the form of B's right to *withhold payment* until there is complete performance by A. Usually, A's non-performance will involve breach, but sometimes his non-performance will be excused on the basis of 'frustration', that is, the result of extreme supervening events beyond his control (for example, see 17.52 concerning *Cutter v. Powell* (1795)). In the event of frustration, A (and A's estate) will be excused: there will be no breach. For example, A might die before fully performing personal services. If so, B can withhold performance, but the Law Reform (Frustrated Contracts) Act 1943 might enable A's estate to gain a 'just sum' in respect of A's incomplete performance (16.25).

17.06 *Strict or non-strict obligations.*¹⁷ Breach of contract can involve failure to satisfy a strict obligation (for example, a seller's statutory obligations to deliver goods which (1) correspond to their contractual description, (2) are of satisfactory quality, and (iii) are reasonably

¹⁵ *Staffordshire Area Health Authority v. South Staffordshire Waterworks Co.* [1978] 1 WLR 1387, CA.

¹⁶ *Ibid.*, at 1406.

¹⁷ For academic discussion, mostly from a US perspective, of the strict nature of many contractual obligations, see various papers in the *Michigan Law Review* symposium on 'Fault in American Contract Law' (2009) 107 *Michigan Law Review* 1431–1600.

fit for their intended purpose).¹⁸ However, some implied contractual obligations require only the exercise of reasonable care, or the meeting of the relevant professional level of diligence.¹⁹ The House of Lords affirmed in *Henderson v. Merrett Syndicates Ltd* (1995)²⁰ (1.23) that, when a contractual duty of care overlaps with an essentially similar duty of care imposed by the tort of negligence (a case of ‘concurrent’ obligations), a claimant can select whichever cause of action he prefers, or indeed plead both (see also the discussion of contributory negligence at 18.50) (there has also been discussion of the ‘contract/tort interface’ in recent US literature).²¹ The Court of Appeal in *Platform Funding Ltd v. Bank of Scotland plc* (2009)²² acknowledged that, in a contract for professional services, the professional will normally merely owe a duty to exercise due care, rather than be under a strict obligation whereby he impliedly guarantees the success of the task. But the court also noted that there can be exceptions based on (1) the specific terms of the agreement, or on a ‘certificate’ or warranty given by the professional in the course of his performance, or (2) the relevant context.²³ The majority (Moore-Bick and Rix LJ; Sir Anthony Clarke MR dissenting) held that, on the facts, a valuer’s failure to inspect the relevant property was a breach of an implied strict obligation to view the relevant property. His certificate, stating that he had inspected the named property, constituted an express warranty (negligence had not been pleaded).²⁴ The dissenting judge, Sir Anthony Clarke MR, said there was no indication in this context that the certificate should trigger strict liability.

Similarly, strict liability was imposed for bug bites suffered by visitor to the Turkish baths in *Silverman v. Imperial London Hotels Ltd* (1927)²⁵ (13.09); conversely, the Court of Appeal found no binding oral guarantee in the ‘unsuccessful vasectomy’ case, *Thake v. Maurice* (1986) (3.71);²⁶ and, in *Easton v. Hitchcock* (1912) (13.09), a private detective service was not liable for breach of confidentiality committed by a former employee, even though the latter’s revelation had wholly undermined the value of the detective work, and even though the defendant’s advertising contained a promise of complete ‘secrecy’.

An illustration of a contractual duty of care is *Evans v. Kosmar Villa Operators* (2008) (13.06).²⁷ The case concerned a tour operator’s duty to take reasonable steps to guard its customers and guests against personal injury, a duty arising both at common law and under statute.²⁸ The Court of Appeal held that this duty did not require the operator to protect a 17-year-old

18 Sections 13–15 of the Sale of Goods Act 1979; G. H. Jones (with P. Schlechtriem), ‘Breach of Contract’, in *International Encyclopedia of Comparative Law*, vol. VII, *Contracts in General* (Tübingen, 1999), 15–16 ff, and 15–204 ff.

19 Generally, section 13 of the Supply of Goods and Services Act 1982.

20 [1995] 2 AC 145, HL; on the topic of concurrent liability, see *Chitty on Contracts* (30th edn, London, 2008), 1–117 ff.

21 R. Kreitner, ‘Fault at the Contract/Tort Interface’ (2009) 107 *Michigan Law Review* 1533.

22 [2008] EWCA Civ 930; [2009] 2 WLR 1016.

23 *Ibid.*, at [48], *per* Rix LJ.

24 *Ibid.*, at [63] (and see [53], *per* Rix LJ).

25 137 LT 57; [1927] All ER 712, 714; 43 TLR 260.

26 [1986] QB 644, CA.

27 [2007] EWCA Civ 1003; [2008] 1 WLR 297.

28 Package Travel, Package Holidays and Package Tours Regulations 1992 (SI 1992 No. 3288), reg. 15.

against the danger of injury caused by diving into the shallow end of a swimming pool. The claimant was aware of the danger.

17.07 Deliberate breach. Lord Wilberforce in the *Suisse Atlantique* case (1966) made clear that deliberate breach of contract is not a special category of breach amounting to ‘fundamental breach’, although (1) an exclusion clause might not be construed to extend this far (‘depending on what the party in breach “deliberately” intended to do, it may be possible to say that the parties never contemplated that such a breach would be excused or limited’), and (2) the fact that a breach is deliberate might be relevant in determining whether the guilty party has evinced an intention no longer to be bound by the contract.²⁹ As for proposition (1), Gabriel Moss QC held in *Internet Broadcasting Corporation Ltd v. MAR LLC* (2009)³⁰ that there is a presumption that an exclusion clause, although literally wide enough to cover this, will not be construed to protect a person (including a company controlled by an identifiable person) from liability for loss of profit flowing from a personal and deliberate repudiation of the relevant contractual undertaking. It is clear that a deliberate breach does not give rise to liability for exemplary damages in English contract law: indeed, exemplary damages are not available at all for breach of contract.³¹ (This topic has stimulated extensive discussion in the USA.)³²

17.08 Nominal or substantial damages. Breach of contract always entitles the innocent party to nominal damages.³³ Such damages are a token sum intended to denote the unlawful nature of the defendant’s act or omission. The innocent party will only be entitled to ‘substantial damages’ (proposition (3) at 18.23) if he can prove that he has suffered loss as a result of the breach.

17.09 Restricted entitlement to terminate for breach. As Lord Porter said in *Heyman v. Darwins Ltd* (1942):³⁴ ‘The three sets of circumstances giving rise to a discharge contract [for breach] are tabulated by *Anson* [in the 1937 edition] as: (1) renunciation by a party of

29 *Suisse Atlantique Société d’Armement Maritime SA v. NV Rotterdamsche* [1967] 1 AC 361, 435, HL (on ‘deliberateness’, see *ibid.*, at 394E, *per* Viscount Dilhorne, 397–8, *per* Lord Reid, 414, *per* Lord Hodson, and 429, *per* Lord Upjohn); R. Brownsword, in C. Mitchell and P. Mitchell (eds.), *Landmark Cases in the Law of Contract* (Oxford, 2008), 299 ff.

30 [2009] EWHC 844 (Ch); [2010] 1 All ER (Comm) 112; [2009] 2 Lloyd’s Rep 295 (see especially the distillation of principles at [33]).

31 *Addis v. Gramophone Co. Ltd* [1909] AC 488, HL; *McGregor on Damages* (18th edn, London, 2009), 11-016; otherwise in Canada, *Royal Bank of Canada v. Got* (2000) 17 DLR (4th) 385 (Supreme Court of Canada); J. Edelman, (2001) 117 LQR 539; *Whiten v. Pilot Insurance Co.* [2002] SCC 18; [2002] 1 SCR 595 (Supreme Court of Canada); as for punitive damages in English tort law, see *Kuddus v. Chief Constable of Leicestershire* [2002] 2 AC 122, HL, and *A v. Bottrill* [2003] 1 AC 449, PC; and for the position in deceit (exemplary damages available, at least in some instances of deceit; but not awarded in this case where the defendant was vicariously liable for another’s deceit), see *Parabola Investments Ltd v. Browallia Cal Ltd* [2009] EWHC 901 (Comm), at [205] ff, *per* Flaux J (point not considered on appeal: [2010] EWCA Civ 486).

32 O. Bar-Gill and O. Ben-Shahar, (2009) 107 *Michigan Law Review* 1479; R. Cresswell, *ibid.*, at 1501; S. Thel and P. Siegelman, *ibid.*, at 1517.

33 Putting aside failure to pay money, for which the action is one for debt: see 18.03 ff.

34 [1942] AC 356, 397, HL.

his liabilities ...; (2) impossibility created by his own act; (3) total or partial failure of performance.' This classification was also adopted by Devlin J in *Universal Cargo Carriers Corporation v. Citati* (1957).³⁵

Thus, the innocent party is entitled to terminate a contract for breach if: (1) the other party has shown a clear unwillingness to satisfy his contract ('renunciation', sometimes known as 'repudiatory breach'); or (2) performance has been rendered impossible by the default of the guilty party; or (3) there has been a breach of an important term (a 'condition') or of another term which can give rise to termination, depending on the seriousness of the breach (an 'innominate term'). Categories (1) and (2) (on which see 17.14) are 'anticipatory' forms of breach (if the other party elects to treat them as such), because each precedes the date for performance

- 17.10 *Terminology: 'termination for breach' and 'rescission' (ab initio).* Termination for breach is to be distinguished from rescission for misrepresentation (or for another 'vitiating' factor, such as duress, undue influence, unconscionability and non-disclosure). Termination for breach brings to an end the parties' 'primary' obligations. However, such termination does not nullify the whole contract. The guilty party's liability to pay compensation also remains. Exclusion and liquidated damages clauses, and arbitration or jurisdiction clauses (17.48), also survive such termination.

2. ANTICIPATORY BREACH

- 17.11 *Anticipatory breach by stating one's unwillingness to perform.*³⁶ Before the date for performance, a party might indicate, whether explicitly or implicitly, that he does not intend to perform. The other party then has a choice whether to accept this and terminate the contract or to try and keep the contract alive. If the renunciation is accepted, the innocent party's cause of action for breach immediately arises. This 'encourages the speedy disposal of broken-down contracts and minimises the innocent party's losses'.³⁷ Anticipatory breach of this type was first recognised only in the mid-nineteenth century. There is a learned survey of this development in Lord Ackner's speech in *'The Simona'* (1989).³⁸

35 [1957] 2 QB 401, 436–8 (the appellate decisions at [1957] 1 WLR 979, CA, and [1958] 2 QB 254, CA, do not disturb the judge's exposition of the governing principles of breach); M. Mustill, *Anticipatory Breach: Butterworths Lectures 1989–90* (London, 1990), 69 ff (see also M. Mustill, (2008) 124 LQR 569–85).

36 For powerful analysis of the whole topic, see M. Mustill, *Anticipatory Breach: Butterworths Lectures 1989–90* (London, 1990), 69 ff, and M. Mustill, (2008) 124 LQR 569–85, at 576 ff; see also J. C. Smith, in E. Lomnicka and C. J. G. Morse (eds.), *Contemporary Issues in Commercial Law: Essays in Honour of A. G. Guest* (London, 1994), 175; G. H. Jones (with P. Schlechtriem), 'Breach of Contract', in *International Encyclopaedia of Comparative Law*, vol. VII, *Contracts in General* (Tübingen, 1999), 15–151 ff; on the nineteenth-century history of this topic, see M. Lobban, in W. Cornish, J. S. Anderson, R. Cocks, M. Lobban, P. Polden and K. Smith, *The Oxford History of the Laws of England*, vol. XII, 1820–1914: *Private Law* (Oxford, 2010), 494 ff.

37 M. Chen-Wishart, *Contract Law* (2nd edn, Oxford, 2008), 497.

38 *Fercometal SARL v. Mediterranean Shipping Co. SA ('The Simona')* [1989] AC 788, 797–805, HL; on US case law and comment, see G. H. Jones (with P. Schlechtriem), 'Breach of Contract', in *International Encyclopaedia of Comparative Law*, vol. VII, *Contracts in General* (Tübingen, 1999), 15–156; Q. Liu, [2007] CLJ 574; *Berkeley Community Villages Ltd v. Pullen* [2007] EWHC 1330 (Ch), Morgan J.

But first let us consider the seminal nineteenth-century cases of *Hochster v. De La Tour* (1853)³⁹ and *Frost v. Knight* (1872).⁴⁰

- 17.12 In *Hochster v. De La Tour* (1853), the defendant engaged the claimant to act as courier on a projected foreign tour, starting on 1 June.⁴¹ On 11 May, just over two weeks before the tour was to begin, the defendant renounced the engagement. It was held that the innocent party had a choice whether to accept the repudiation, or to keep the contract alive pending the date for due performance. There would be no ‘breach’ if the innocent party decided not to accept the repudiation. In the present case, the claimant was entitled to seek damages immediately, once he had accepted this renunciation. It was not necessary for him to wait to see whether the defendant might change his mind.
- 17.13 *Frost v. Knight* (1872)⁴² concerned an agreement to marry (since 1970, such an agreement is no longer actionable).⁴³ The defendant had agreed to marry the claimant, once the defendant’s father had died. The defendant broke off the engagement before his father’s death. Cockburn CJ said that this renunciation became a breach once the innocent party ‘treated the undertaking as broken’. Thus, the peculiarity of this form of default is that the guilty party’s announcement only becomes wrongful if the other party decides that he will respond by calling off the contract. The innocent party can then demand compensation.
- 17.14 *Disablement at the ‘anticipatory’ stage: impossibility by culpable self-inducement.* Another form of anticipatory breach is where the guilty party incapacitates himself or prevents performance before the scheduled date. This need not involve deliberate sabotaging of the contract. It is enough that the default involves breach of an express or implied term. This category is amongst Lord Porter’s classification (noted at 17.09) in *Heyman v. Darwins Ltd* (1942):⁴⁴ ‘impossibility created by his own act’. But, as Devlin J observed in *Universal Cargo Carriers Corporation v. Citati* (1957),⁴⁵ a decision to justify termination on this basis involves the ‘serious risk’ that the court might find that in fact the other party’s inability to perform had not been shown to be inevitable (see the next case).

The danger of too readily and unsafely inferring the other party’s complete incapacitation is illustrated by *Alfred Toepfer International GmbH v. Itex Itagrani Export SA* (1993).⁴⁶ The seller prematurely calculated that the buyer would be unable to load a cargo

39 (1853) 2 E & B 678; 22 LJ (QB) 455.

40 (1872) LR 7 Ex 111.

41 (1853) 2 E & B 678; 22 LJ (QB) 455; P. Mitchell, in C. Mitchell and P. Mitchell (eds.), *Landmark Cases in the Law of Contract* (Oxford, 2008), 135.

42 (1872) LR 7 Ex 111; M. Mustill, (2008) 124 LQR 569, 577, noting G. Frost, *Promises Broken: Courtship, Class, and Gender in Victorian England* (Charlottesville, VA, 1995).

43 Since 31 December 1970: section 1(1) of the Law Reform (Miscellaneous Provisions) Act 1970.

44 [1942] AC 356, 397, HL.

45 [1957] 2 QB 401, 436–8 (the appellate decisions at [1957] 1 WLR 979, CA, and [1958] 2 QB 254, CA, do not disturb the judge’s exposition of the governing principles of breach); M. Mustill, *Anticipatory Breach: Butterworths Lectures 1989–90* (London, 1990), 69 ff; M. Mustill, (2008) 124 LQR 569, 580 n. 23, notes the galaxy of commercial talent employed in arguing this case.

46 [1993] 1 Lloyd’s Rep 360, Saville J.

in full. But the court held that in fact it was not at all certain that the buyer would have failed to do so. In the absence of such a justification, the seller was held to have repudiated. Saville J said the relevant test is whether:⁴⁷

on the balance of probabilities the party in question cannot perform his obligations. The fact that that party has entered into inconsistent obligations does not in itself necessarily establish such inability, unless those obligations are of such a nature or have such an effect that it can truly be said that the party in question has put it out of his power to perform his obligations.

Saville J added:⁴⁸

In the present case, however, the mere fact that the sub-buyers had contracted to load other goods on the vessel did not, in itself, establish that the buyers could not perform – at most that established that the buyers might not be able to perform ... [I]t could not be said that the buyers had on the face of it or otherwise put it out of their power to perform ... [I]n the present case there was only a chance that the buyers would be unable to perform.

To avoid this danger, the prudent course is to contend instead that the other party has *expressly renounced* the contract.

There is an attractive provision in PECL, the *Principles of European Contract Law*.⁴⁹ Article 8:105 ('Assurance of performance') provides:

(1) A party which reasonably believes that there will be a fundamental non-performance by the other party may demand adequate assurance of due performance and meanwhile may withhold performance of its own obligations so long as such reasonable belief continues.

(2) Where this assurance is not provided within a reasonable time, the party demanding it may terminate the contract if it still reasonably believes that there will be a fundamental non-performance by the other party and gives notice of termination without delay.

UNIDROIT's *Principles of International Commercial Contracts* (2004), Article 7.3.4,⁵⁰ and the US Uniform Commercial Code, section 2-609(1),⁵¹ contain similar provisions. But, under English law, a party has no right to demand such an assurance from the other

⁴⁷ *Ibid.*, at 362.

⁴⁸ *Ibid.*

⁴⁹ T. Naudé, in H. MacQueen and R. Zimmermann (eds.), *European Contract Law: Scots and South African Perspectives* (Edinburgh, 2006), chapter 11.

⁵⁰ 2nd edn, Rome, 2004; see M. J. Bonell (ed.), *The UNIDROIT Principles in Practice: Case Law and Bibliography on the UNIDROIT Principles of International Commercial Contracts* (2nd edn, Ardsley, NY, 2006), 385 ff; S. Vogenauer and J. Kleinheisterkamp (eds.), *Commentary on the UNIDROIT Principles of International Commercial Contracts* (Oxford, 2009), 849 ff.

⁵¹ G. H. Jones (with P. Schlechtriem), 'Breach of Contract', in *International Encyclopaedia of Comparative Law*, vol. VII, *Contracts in General* (Tübingen, 1999), 15-153.

side.⁵² The non-English rules, just mentioned, are attractive because they enable a party to gain protection when he reasonably apprehends that the other party's major default is, if not inevitable, certainly a genuine source of anxiety.

- 17.15 *Innocent party's decision to maintain the contract and sue for agreed remuneration.* The House of Lords majority decision in *White & Carter v. McGregor* (1962)⁵³ establishes that, occasionally, the innocent party might have the capacity to keep open the contract (the right to 'affirm the contract'), and complete his side of the bargain. He can then sue for the agreed price. But some cases have qualified this and prevented the innocent party from saddling the other party with unwanted performance (for details, see 18.05 ff).

3. RENUNCIATION AT THE DATE OF PERFORMANCE

- 17.16 *Good reason exists for termination but the wrong reason was invoked at the time.* It is a 'long-established rule'⁵⁴ that, even though A *thinks that he has committed a breach*, he will not in fact have done so if he was in fact entitled to terminate the contract because of the other party's serious breach or repudiation of the contract.⁵⁵

The Court of Appeal in *Glenmore Grain Rotterdam BV v. Lebanese Organisation for International Commerce* (1997) acknowledged that protection of party A is subject to two qualifications:⁵⁶ first, party A's failure to take the correct point is fatal if party B could have put right this default within the contractual deadline if B had been notified by A of the relevant default;⁵⁷ secondly, estoppel by conduct or representation might render it unjust for party A, the innocent party, to invoke the true ground if party B has altered his position in a harmful fashion.⁵⁸

- 17.17 *A party's mistaken but good-faith statement that his non-performance is justified.* This is the converse situation of the previous case. A party genuinely, but mistakenly, believes that he is entitled not to perform: can this amount to renunciation?⁵⁹ The answer to this question is 'yes': a statement of unwillingness to perform made in good faith but without legal justification will constitute a breach, especially if the statement is made at the time of performance. Thus, in *Federal Commerce & Navigation Co. v. Molena Alpha Inc.* (1979), a ship-owner refused to issue prepaid bills of lading. He was acting on inaccurate legal advice. In fact, he had no right to refuse to do so. As a result of the owner's refusal, the

52 J. Carter, 'Suspending Contract Performance for Breach', in J. Beatson and D. Friedmann (eds.), *Good Faith and Fault in Contract Law* (Oxford, 1995), 485, 487–8, citing authorities.

53 [1962] AC 413, HL.

54 *Taylor v. Oakes Roncoroni & Co.* (1922) 127 LT 267, 269, *per* Greer J (KBD and CA).

55 *Ibid.*; see also '*The Mihalios Angelos*' [1971] 1 QB 164, 195–6, 204, CA.

56 [1997] 4 All ER 514, CA.

57 *Ibid.*, at 526 (noting *Heisler v. Anglo-Dal Ltd* [1954] 1 WLR 1273, 1278, CA).

58 *Glenmore Grain* case, [1997] 4 All ER 514, 530–1, CA, noting *Panchaud Frères SA v. Etablissements General Grain Co.* [1970] 1 Lloyd's Rep 53, CA (the latter case contains loose *dicta*, especially by Winn LJ at 59).

59 G. H. Jones (with P. Schlechtriem), 'Breach of Contract', in *International Encyclopaedia of Comparative Law*, vol. VII, *Contracts in General* (Tübingen, 1999), 15–152.

charterer could not use the ship. The House of Lords held that the ship-owner's refusal involved repudiation.⁶⁰ It did not matter that the ship-owner had in good faith misinterpreted its legal position. Lord Denning MR's comment in the *Federal Commerce* case⁶¹ (affirmed by the House of Lords in the same case) was later adopted by Lord Woolf in the Privy Council in the *Vaswani* case (1996).⁶² Lord Woolf said:

Nor is conduct, if it is repudiatory, excused because it occurs in consequence of legal advice, as may be the case with the sellers' actions in this case. The position is correctly set out by Lord Denning MR in the *Federal Commerce* case,⁶³ in a passage of his judgment cited by Lord Scarman in *Woodar Investment Development Ltd v. Wimpey Construction UK Ltd*.⁶⁴ [Lord Denning's statement] is in these terms:

'I have yet to learn that a party who breaks a contract can excuse himself by saying that he did it on the advice of his lawyers; or that he was under an honest misapprehension ... I would go by the principle ... that if the party's conduct – objectively considered in its impact on the other party – is such as to evince an intention no longer to be bound by his contractual obligations, then it is open to the other party to accept his repudiation and treat the contract as discharged from that time onwards.'

But it is possible that the court will not find an actionable repudiation if the erroneous statement precedes the date for performance, as in the *Woodar* case (1980).⁶⁵

In that case, the claimant had agreed to sell land to the defendant. Completion was to occur after gaining planning permission. The defendant purchaser resiled from the deal, invoking in good faith, but mistakenly, a purported contractual right to withdraw. In fact, the defendant had no such right. The majority (Lords Wilberforce, Keith and Scarman; Lords Salmon and Russell dissenting) held that the defendant had not absolutely refused to perform. Instead, the defendant was purporting to rely (albeit wrongly) on an escape clause. It had not 'made a stand' at the date of completion but in advance of it.

The statement, even if wrong, must be repudiatory: it must potentially concern a matter which will wreck the whole deal. Thus, even if the allegedly repudiatory statement occurs at, or very close to, the time for performance, the Privy Council in the *Vaswani* case (1996) emphasised that the court will consider whether the addressee's reasonable interpretation of the other's words or conduct was that the contract was being abandoned and was no longer open for performance.⁶⁶ The test proposed by the Privy Council is this:⁶⁷

60 [1979] AC 757, HL.

61 *Federal Commerce & Navigation Co. v. Molena Alpha Inc.* [1978] QB 927, 979, CA.

62 [1996] 1 WLR 270, 277, PC, Lord Woolf.

63 *Federal Commerce* case, [1978] QB 927, 979, CA.

64 [1980] 1 WLR 277, 298, HL.

65 *Ibid.*

66 [1996] 1 WLR 270, 276–7, PC, Lord Woolf; noted by E. Peel, [1996] LMCLQ 309.

67 [1996] 1 WLR 270, 276–7, PC.

[I]f the [guilty party's] conduct ... went beyond the assertion of a genuinely held view of the effect of the contract, the conduct could amount to a repudiation. This is the position if the conduct is inconsistent with the continuance of the contract. Then the *bona fide* motives of the party responsible do not prevent the conduct being repudiatory.

In the *Vaswani* case (1996), the sellers had purported to increase the price payable for the purchase of a Ferrari Testarossa sports car (from £179,500 to £218,800). It turned out that the terms of the contract did not justify this unilateral increase. But the Privy Council held that this did not amount to repudiation. Therefore, the purchaser had not been entitled to rescind from the transaction, using the price error as his pretext. And so the seller was entitled to retain the deposit (£44,875). Lord Woolf emphasised that the sellers had not put forward their (unjustified) increase on a 'take it or leave it' basis, and the buyer had not sought to challenge the figure in an open fashion.

4. TERMINATING FOR BREACH OF CONDITION OR OTHER SERIOUS BREACH

- 17.18 *Classification of promissory terms.* There are three types of promissory obligation: conditions; innominate (or 'intermediate') terms; and warranties.⁶⁸ There is no fourth category of 'fundamental term'.⁶⁹ Breach of a condition entitles the other party to obtain damages and to terminate for breach of contract. Breach of an intermediate term also entitles the innocent party to claim damages; whether it also justifies termination of the contract depends on an assessment of the breach's gravity on the particular facts. But breach of a warranty gives rise only to a duty to pay damages (commenting on warranties, *Chitty on Contracts* suggests⁷⁰ that the emergence of innominate terms (17.30 ff) has probably reduced this category to vanishing point, 'save in the very exceptional circumstances where a term has been specifically so classified by statute').⁷¹ It becomes crucial, therefore, to determine whether a particular contractual obligation should be classified as a condition, an innominate term or a warranty. Often the categorisation, established by reference to the factors discussed at 17.19, is clear and works satisfactorily. However, sometimes this can become a perplexing question, and it can divide judges at the highest level (notably *Schuler (L) AG v. Wickman Machine Tool Sales Ltd* (1974) (17.20 ff)).

68 On the history of warranties and conditions, see D. J. Ibbetson, *A Historical Introduction to the Law of Obligations* (Oxford, 1999), 83–7; G. H. Jones (with P. Schlechtriem), 'Breach of Contract', in *International Encyclopaedia of Comparative Law*, vol. VII, *Contracts in General* (Tübingen, 1999), 15–129 ff; M. Lobban, in W. Cornish, J. S. Anderson, R. Cocks, M. Lobban, P. Polden and K. Smith, *The Oxford History of the Laws of England*, vol. XII, 1820–1914: *Private Law* (Oxford, 2010), 485 ff.

69 *Suisse Atlantique Société d'Armement Maritime SA v. NV Rotterdamsche* [1967] 1 AC 361, HL; *Photo Production Ltd v. Securicor Transport Ltd* [1980] AC 827, HL; on the fundamental breach saga, see *Chitty on Contracts* (30th edn, London, 2008), 12–021 to 12–024 and 14–020 to 14–024.

70 *Chitty on Contracts* (30th edn, London, 2008), 12–031.

71 E.g. sections 11(3) and 12(2), (4), (5) and (5A) of the Sale of Goods Act 1979 (as amended) and section 8(3) of the Supply of Goods (Implied Terms) Act 1973 (as amended).

17.19 *When is a term a 'condition'?* A term is a condition, rather than one of the other two kinds of promissory term, in any of the following five situations:

- (1) statute explicitly classifies the term in this way;⁷²
- (2) there is a binding judicial decision supporting classification of a particular term as a 'condition';
- (3) a term is described in the contract as a 'condition' and upon construction it has that technical meaning;
- (4) the parties have explicitly agreed that breach of that term, no matter what the factual consequences, or perhaps breach of any term (again irrespective of the consequences), will entitle the innocent party to terminate the contract for breach; or
- (5) as a matter of general construction of the contract, the clause is to be understood to be intended to operate as a condition.

This classification was declared as 'neat' by Waller LJ in *'The Seaflower'* (2001),⁷³ who adopted the statement by *Chitty on Contracts* (although it should be noted that *Chitty* does not separate items (3) and (4) in this list).⁷⁴ Of these five situations, the last four will now be explained in detail.

(2) *There is a binding judicial decision supporting this classification of a particular term as a 'condition'.*

In *'The Mihalis Angelos'* (1971), the Court of Appeal categorised as a condition an owner's statement in a charterparty that the vessel was 'expected ready to load under this charter about [a specified date]'.⁷⁵

In *Bunge Corporation v. Tradax Export SA* (1981), the House of Lords also treated as a condition a clause requiring the buyer to give at least fifteen days' notice to the seller of the buyer's intention to ship the goods, whereupon the seller could decide which port to use for the shipment.⁷⁶ The transaction was part of a 'string' of contracts for the transfer of these goods.

In *Compagnie Commerciale Sucre et Denrees v. C Czarnikow ('The Naxos')* (1990), the House of Lords held that a condition had been created when a clause required the sellers to have goods ready for delivery on the arrival of the vessel at port.⁷⁷

In *BS & N Ltd (BVI) v. Micado Shipping Ltd (Malta) ('The Seaflower')* (2001), the Court of Appeal categorised as a condition a clause requiring the owners to obtain approval, within sixty days,

72 E.g. sections 12(5A), 13(1A), 14(6) and 15(3) of the Sale of Goods Act 1979 (as amended); in non-consumer cases, sections 13–15 must be read subject to section 15A.

73 *BS & N Ltd (BVI) v. Micado Shipping Ltd (Malta) ('The Seaflower')* [2001] 1 Lloyd's Rep 341, at [42].

74 *Chitty on Contracts* (30th edn, London, 2008), 12-040.

75 [1971] 1 QB 164, CA.

76 [1981] 1 WLR 711, HL.

77 [1990] 1 WLR 1337, HL; noted by M. Clarke, [1991] CLJ 29.

from a specified oil company, Exxon, that the latter consented to use of the relevant vessel.⁷⁸ The court held that this was a condition, entitling the charterer to terminate the contract once it became apparent that Exxon's approval had not been obtained within the sixty-day period. This was so, even though the clause did not contain an explicit right of cancellation, by contrast with other provisions of the charterparty (failure to maintain the approval of four other oil companies, whose approval had already been given).

In *Barber v. NWS Bank plc* (1996), the Court of Appeal held that a hire-purchase dealer had breached a condition that he would have title to a car which was sold (conditionally) to the claimant on hire-purchase.⁷⁹

(3) *A term is described in the contract as a 'condition' and upon construction it has that technical meaning.* The House of Lords decision in the *Schuler* case (1974)⁸⁰ (17.20 ff) indicates that the courts will give effect to the word 'condition', treating it as a promissory condition entitling the innocent party to terminate the contract, unless the court is persuaded that the parties could not possibly have intended this, because such a meaning would lead to manifest absurdity or complete unreasonableness. But it is submitted that such a decision to 'downgrade' the word 'condition' to an intermediate term should not be made unless there is strong support for the inference that 'condition' was not intended to have this technical meaning.

(4) *The parties have explicitly agreed that breach of that term, no matter what the factual consequences, or perhaps breach of any term (again irrespective of the consequences), will entitle the innocent party to terminate the contract for breach.*⁸¹ Here, the word 'condition' has not been used, but a longer expression has been adopted. However, the Court of Appeal in the *Rice* case⁸² (17.25) held that such a termination provision will not always be taken literally if this will lead to manifest absurdity (that is, if it would 'fly in the face of commercial common sense').

(5) *General construction of the contract.* The following quotation, from *Chitty*,⁸³ was endorsed by Lords Wilberforce and Roskill in *Bunge v. Tradax* (1981):⁸⁴

[T]he nature of the contract or the subject matter or the circumstances of the case might support the conclusion that the parties must, by necessary implication, have intended that the innocent party would be discharged from further performance of his obligations in the event that the term was not fully and precisely complied with.

⁷⁸ [2001] 1 Lloyd's Rep 341, CA.

⁷⁹ [1996] 1 WLR 641, 646, CA.

⁸⁰ [1974] AC 235, HL.

⁸¹ *Lombard North Central plc v. Butterworth* [1987] QB 527, CA.

⁸² *Rice v. Great Yarmouth Borough Council*, *The Times*, 26 July 2000; (2001) 3 LGLR 4, CA.

⁸³ *Chitty on Contracts* (30th edn, London, 2008), 12-040.

⁸⁴ *Bunge Corporation New York v. Tradax SA* [1981] 1 WLR 711, 715-16, 726, HL (also citing Lord Diplock in *Photo Production v. Securicor Transport Ltd* [1980] AC 822, 840, HL).

Diplock LJ unsuccessfully suggested in the *Hongkong Fir* case (1962) that, unless the relevant clause has been classified by legislation or the parties' own provision as a condition, the innocent party is entitled to terminate for breach only if the consequences of breach have been very serious indeed.⁸⁵ But this is wrong. Later cases show that the courts are prepared to classify a promissory term as a condition even though the contract does not so explicitly categorise the term in this way. This was confirmed by Lord Wilberforce in *Bunge v. Tradax* (1981), who made clear that the courts can, in appropriate circumstances, find that a term is to operate as a condition, even though the contract has not explicitly stipulated this.⁸⁶

- 17.20 'Condition' not always used in technical sense. By a majority, the House of Lords in *Schuler (L) AG v. Wickman Machine Tool Sales Ltd* (1974) held that, on proper construction of the contract, the word 'condition' might not have been intended to operate in a technical sense; therefore, breach of the relevant obligation does not necessarily justify termination.⁸⁷ Lord Wilberforce dissented. The facts were as follows.

W agreed to act as a distribution agent for S, a German manufacturer. Clause 7(b) required W to send a representative at least once a week to six specified motor manufacturers. W had committed itself to making roughly 1,400 visits over a four-and-a-half-year period to solicit orders for 'panel pressers' (equipment used in the manufacture of vehicles). This clause was labelled a 'condition'. Another clause, 11(a)(1), allowed a party to terminate the contract in the event of a 'material breach', provided the relevant breach had not been remedied within sixty days after the aggrieved party had given written notice. S sought to bypass this clause, and instead purported to terminate the contract on the basis of breaches of clause 7(b). S had waived earlier defaults. But W consistently failed to make significant percentages of the stipulated visits.

In the Court of Appeal, Lord Denning MR had chronicled the facts as follows:⁸⁸

May 1, 1963, to January 13, 1964

The arbitrator found that during this period there were failures by Wickman Sales to visit the six firms as required by clause 7, and that these failures were a material breach of the obligation ... [But the Court of Appeal held that 'there was a waiver by Schulers of their rights in respect of breaches antecedent to January 13, 1964']

January 13, 1964, to July 13, 1964

[Out] of 144 weekly visits to the six firms, only 15 were missed. The arbitrator found that these failures were not a material breach ...

⁸⁵ [1962] 2 QB 1, 69–70, CA.

⁸⁶ *Bunge Corporation New York v. Tradax SA* [1981] 1 WLR 711, 715–16, HL.

⁸⁷ [1974] AC 235, HL; noted by J. H. Baker, [1973] CLJ 196, R. Brownsword, (1974) 37 MLR 104, and F. A. Mann, (1973) 89 LQR 464.

⁸⁸ [1972] 1 WLR 840, 847–8, CA.

July 14, 1964, to October 27, 1964

Out of 96, only nine were missed. These were for good reasons, as, for instance, four because the works were shut down, and two because the firms went to visit Wickmans at their 'At Homes', and so forth. The arbitrator found that these failures were not a material breach.

The arbitrator had held that the word 'condition' had not been used in its technical sense and that it was necessary for S to show a material breach by W. He found that there had been one period of material breach (before 13 January 1964), but that this had been waived. Later periods of default were held by him to have fallen short of material breach. Mocatta J reversed this, holding that the word 'condition' had been used in a technical sense.

The Court of Appeal by a majority (Lord Denning MR and Edmund-Davies LJ; Stephenson LJ dissenting) held that the word 'condition' had not been used in a technical sense and that the waiver point should be upheld. This meant there had been no period of material breach.

The House of Lords, as we shall see, agreed that 'condition' had not been used in a technical sense, and agreed with the other aspects of the Court of Appeal's decision. But Lord Wilberforce dissented.

It is submitted that the case is better explained as turning on the fact that two clauses – clause 7 and clause 11 – were very hard to reconcile. For this reason – a problem of internal consistency – the clause containing the word 'condition' was construed as not having been used in its technical sense (see 17.21). In short, the House of Lords gave priority to clause 11 (allowing a party to terminate the contract in the event of a 'material breach', provided the relevant breach had not been remedied within sixty days after the aggrieved party had given written notice (this point is expanded at 17.21); but for scepticism, see Lord Wilberforce's dissent (17.23)).

The principle that the whole contract must be considered when interpreting a particular clause, phrase or word is a cardinal feature of interpretation under English law: see, notably, the *Sigma* (2009)⁸⁹ and the *Charter Reinsurance* (1997)⁹⁰ cases (discussed at 14.12). The same approach is recognised in the (non-binding) codes: PECL, *Principles of European Contract Law*, Article 5:105; and UNIDROIT's *Principles of International Commercial Contracts* (2004), Article 4.4.⁹¹

- 17.21** *Internal inconsistency; 'condition' downgraded.* The main route to the majority's decision in the *Schuler* case held that the word 'condition' should not be read in its 'strict

⁸⁹ *In Re Sigma Finance Corporation (in administrative receivership)* [2009] UKSC 2; [2010] 1 All ER 571; [2010] BCC 40.

⁹⁰ Lord Mustill in *Charter Reinsurance Co. Ltd v. Fagan* [1997] AC 313, 384, HL, quoted in the *Sigma* case, *ibid.*, at [9].

⁹¹ On the UNIDROIT principle, see M. J. Bonell (ed.), *The UNIDROIT Principles in Practice: Case Law and Bibliography on the UNIDROIT Principles of International Commercial Contracts* (2nd edn, Ardsley, NY, 2006), 238–9; S. Vogenauer and J. Kleinheisterkamp (eds.), *Commentary on the UNIDROIT Principles of International Commercial Contracts* (Oxford, 2009), 521 ff.

sense',⁹² and that 'condition' in clause 7 should be linked (somewhat clumsily) with the reference elsewhere in the agreement (clause 11) to 'material' breach. Lord Reid hesitatingly concluded that a spate of failed visits could be (partly) 'remedied' in the sense that the agent could 'put his house in order' and reform its 'system' of future visits. And so the sixty-day notice period to remedy had to be complied with. The German company had not been justified in terminating the contract on these facts. Lord Kilbrandon said:⁹³

On the whole, though without a great deal of confidence, I come to the conclusion that the use of the word 'condition' in 7(b) was not intended by the parties to isolate an individual fundamental term, and to provide for [termination], on any breach, in addition to the other more general provisions for [termination] set out in clause 11, without the opportunity being given to the party at fault by clause 11 to put things right for the future, where the nature of the breach made that possible. Thus, when the appellants first had reason to complain in January 1963 of material breaches of clause 7(b), they could have called upon the respondents to make better arrangements within 60 days, upon pain of [termination]. It is only in this way that I can give any meaning to the remedial provision.

17.22 Interpretation to avoid a wholly unreasonable result: 'condition' downgraded. Another strand to the reasoning in the *Schuler* case concerns the prospect of termination for an isolated and unexcused failure to make a visit. Lord Reid suggested that the technical meaning on the present facts would lead to a 'very' unreasonable result, for it would justify termination for any single missed visit, unless the failure was excusable. Lord Reid said:

[T]he fact that a particular construction leads to a very unreasonable result must be a relevant consideration. The more unreasonable the result the more unlikely it is that the parties can have intended it.⁹⁴

It is submitted that such a construction is justified only quite exceptionally, when it would lead to a *very or wholly* unreasonable result. Furthermore, it appears that Lord Reid would have construed the word 'condition' in its technical sense if it had not been necessary to reconcile this clause and the sixty-day notice procedure mentioned in clause 11 (17.21). Although Lord Reid's reference to complete unreasonableness appears not to have been a central plank of the majority's reasoning, his comment has been received into the 'canon' of interpretative 'rules of thumb', as noted by Lord Mustill in *Charter Reinsurance Co. Ltd v. Fagan* (1997) (see further on that case, 14.09).⁹⁵

The words of Lord Reid in [the *Schuler* case] do, of course, reflect not only a method of constructing contracts but also the common experience of how language is understood.

⁹² [1974] AC 235, HL.

⁹³ *Ibid.*, at 271.

⁹⁴ *Ibid.*, at 251, *per* Lord Reid.

⁹⁵ [1997] AC 313, 387–8, HL.

Lord Mustill continued:

This practical rule of thumb (if I may so describe it without disrespect) must however have its limits. There comes a point at which the court should remind itself that the task is to discover what the parties meant from what they have said, and that to force upon the words a meaning which they cannot fairly bear is to substitute for the bargain actually made one which the court believes could better have been made. This is an illegitimate role for a court. Particularly in the field of commerce, where the parties need to know what they must do and what they can insist on not doing, it is essential for them to be confident that they can rely on the court to enforce their contract according to its terms.

- 17.23 *Dissent in the Schuler case (1974)*. Lord Wilberforce, who dissented, concluded that the word ‘condition’ should be applied in its ordinary legal and technical sense; and it would justify termination for unexcused failure to make all agreed visits. In his view, the majority’s approach relaxed the discipline of this commercial agreement, which he robustly described as demanding ‘aggressive, insistent punctuality and efficiency’. He said:⁹⁶

[T]o call [clause 7(b)] arbitrary, capricious or fantastic, or to introduce as a test of its validity the ubiquitous reasonable man (I do not know whether he is English or German) is to assume, contrary to the evidence, that both parties to this contract adopted a standard of easygoing tolerance rather than one of aggressive, insistent punctuality and efficiency. This is not an assumption I am prepared to make, nor do I think myself entitled to impose the former standard upon the parties if their words indicate, as they plainly do, the latter. I note finally, that the result of treating the clause, so careful and specific in its requirements, as a term is, in effect, to deprive the appellants of any remedy in respect of admitted and by no means minimal breaches. The arbitrator’s finding that these breaches were not ‘material’ was not, in my opinion, justified in law in the face of the parties’ own characterisation of them in their document: indeed the fact that he was able to do so, and so leave [Schuler] without remedy, argues strongly that the legal basis of his finding – that clause 7(b) was merely a term – is unsound.

But Lord Wilberforce on this occasion was a solitary hawk, outnumbered in the Lords by a quartet of doves (in the lower courts, however, Lord Wilberforce’s strict approach had been favoured by Mocatta J – on appeal from the arbitrator – and by Stephenson LJ, dissenting in the Court of Appeal).

- 17.24 *The Schuler case (1974) not an example of trivial breach*. The majority’s *reductio ad absurdum* of the single unexcused missed visit certainly distorts the degree of default in the *Schuler* case itself. The amount of default was scarcely negligible (at 17.20, it was shown that between 13 January and 27 October 1964, 18 out of 240 visits were missed

96 [1974] AC 235, 263, HL.

for no good reason). It is also submitted that the German company might have been entitled to terminate the contract by contending that the repeated failures to make visits during the relevant period constituted a renunciation of the contract, and that the sixty-day notice period should not clog the innocent party's common law right to terminate the contract on that basis (for this analysis, see 17.38). It might have been necessary to consider (1) the ratio of the breach to the contract as a whole and (2) the likelihood – as it would seem to a reasonably situated person – of repetition. Lord Hewart CJ in *Maple Flock Co. Ltd v. Universal Furniture Products (Wembley) Ltd* (1934) articulated these two factors in the context of a failure to make deliveries of goods in an agreed set of instalments.⁹⁷ Returning to the problem in the *Schuler* case, the 'renunciation' analysis would have avoided the need to pore over the meaning of 'condition' in the relevant clause. However, the House of Lords' speeches did not address this matter. Finally, Whittaker has noted that facts similar to the *Schuler* case would now fall within the Commercial Agents (Council Directive) Regulations 1993. And he suggests that the courts would now 'feel much less ready to "read down" a term named by the parties as a "condition" [within that new statutory context]'.⁹⁸

- 17.25** *Termination clauses: spelling out the possibility of termination.* The *Schuler* decision (1974) shows that the word 'condition' might sometimes be construed as a 'term'. Therefore, the safer course is for contractual draftsmen to *spell out the innocent party's unqualified right to terminate for any breach of the relevant obligation*. However, the Court of Appeal's decision in *Rice v. Great Yarmouth Borough Council* (2000) reveals that achieving such an unqualified right to terminate the contract requires very careful drafting indeed.⁹⁹ In the *Rice* case (2000), the claimants had entered into a four-year contract to maintain the defendant local authority's sports facilities. The written contract gave the local authority the right to terminate for 'breach of any of [Rice's] obligations under the Contract'. The defendant terminated the contract because of shortcomings in the contractor's performance. In response, the claimant sought damages, alleging that the termination had not been justified. The Court of Appeal found for the claimant. The court held that, despite its literal wording, the relevant clause, just quoted, did not authorise termination for breach of 'any' obligation. In the court's view, such a literal interpretation would impose a 'draconian' contractual regime,¹⁰⁰ and it would 'fly in the face of commercial sense'. Instead, the court concluded that termination would be justified only if there had been 'repudiation' of the overall contract by a pattern of breaches.¹⁰¹ But no such renunciation arose here because the breaches had not been cumulatively serious enough.

97 [1934] 1 KB 148, 156–7, CA, *per* Lord Hewart CJ; *Regent OHG Aisestadt v. Francesco of Jermyn Street Ltd* [1981] 3 All ER 327, Mustill J; section 31(2) of the Sale of Goods Act 1979.

98 S. Whittaker, 'Termination Clauses', in A. Burrows and E. Peel (eds.), *Contract Terms* (Oxford, 2007), chapter 13, at 267–73.

99 *The Times*, 26 July 2000; (2001) 3 LGLR 4, CA.

100 *Ibid.*, at [22], *per* Hale LJ.

101 *Ibid.*, at [17], *per* Hale LJ.

- 17.26 *Commentators' criticisms of the Rice case.* Chen-Wishart has criticised the result in this case:

[T]he decision is questionable; it renders the termination clause meaningless since [the innocent party] can already terminate for a repudiatory breach under general law ... [T]he courts' aversion to interpretations which lead to very unreasonable results is ... motivated by ... avoidance of harsh outcomes which defeat parties' reasonable expectations.¹⁰²

Whittaker's careful analysis of the case¹⁰³ also concludes with this criticism: '[I]ts approach will encourage ever more elaborate attempts to set out a wide power of termination ("termination for any breach, whether material, trivial or otherwise of the obligations set out in clauses A, B, or C").'¹⁰⁴ And Burrows has posed the question whether a clause would be upheld if it provided that termination would be justified for 'any breach, however trivial'.¹⁰⁵ It would indeed be a bold decision for the courts to override this clear language. If the parties are commercial parties, the principle of freedom of contract (1.08 ff) surely requires the courts to accede to such a phrase and not to override it in the name of 'commercial common sense' or by suggesting that a commercial party has submitted to a 'draconian' regime. It is important to recall Lord Mustill's comment in *Charter Reinsurance Co. Ltd v. Fagan* (1997) that it is illegitimate for courts or arbitrators to 'force upon the words a meaning which they cannot fairly bear', since this would be 'to substitute for the bargain actually made one which the court believes could better have been made' (17.22).¹⁰⁶

- 17.27 *The Antaios case (1985): the House of Lords precursor to the Rice case (2000).* The Court of Appeal in the *Rice* case (see 17.25) followed the 'purposive' approach to the contractual phrase 'any other breach' approved by the House of Lords in *Antaios Compania Naviera SA v. Salen Rederierna AB* (1985).¹⁰⁷

The *Antaios Compania Naviera SA* case concerned a charterparty. One of its clauses permitted the owner to terminate the charterparty for 'any' breach committed by the charterer. Lord Diplock, giving the House of Lords judgment on this point, held that this should not be construed to permit termination for a minor breach – inaccuracy in bills of lading submitted to the owner by the charterer. Instead, the clause should be understood to apply only to a repudiatory breach. He said (upholding the arbitrators' award):

102 M. Chen-Wishart, *Contract Law* (2nd edn, Oxford, 2008), 512.

103 S. Whittaker, 'Termination Clauses', in A. Burrows and E. Peel (eds.), *Contract Terms* (Oxford, 2007), chapter 13, at 273–83; Whittaker's chapter contains valuable discussion of many related decisions concerning 'material breach' and similar contract drafting.

104 *Ibid.*, at 283.

105 A. S. Burrows, *A Casebook on Contract* (2nd edn, Oxford, 2009), 331.

106 [1997] AC 313, 388, HL.

107 [1985] AC 191, 200–1, HL.

The arbitrators decided ... that 'any other breach of this charter party' in the withdrawal clause means a repudiatory breach ... such as would entitle the ship-owners to elect to treat the contract as wrongfully repudiated by the charterers, a category into which in the arbitrators' opinion the breaches complained of did not fall ... To the semantic analysis ... the arbitrators added an uncomplicated reason based simply upon business commonsense: 'the owners' construction is wholly unreasonable, totally uncommercial and in total contradiction to the whole purpose of the ... time charter form. The owners relied on what they said was 'the literal meaning of the words in the clause'. We would say that if necessary, in a situation such as this, a purposive construction should be given to the clause so as not to defeat the commercial purpose of the contract.

- 17.28 '*Time of the essence*'.¹⁰⁸ In *Lombard North Central plc v. Butterworth* (1987), Mustill LJ noted:¹⁰⁹ 'A stipulation that time is of the essence, in relation to a particular contractual term, denotes that timely performance is a condition of the contract. The consequence is that delay in performance is treated as going to the root of the contract, without regard to the magnitude of the breach.' The question of timely performance is especially important in conveyancing transactions,¹¹⁰ and contracts of hire containing stipulations for punctual payment (as in the *Lombard* case). The courts are keen to give effect to such provisions where they perceive that commercial certainty is promoted (17.19 at (5), discussing *Bunge v. Tradax* (1981)).¹¹¹ It is also possible for an innocent party to notify the other, who is in breach, that performance must occur within a reasonable time.¹¹²
- 17.29 There is an equitable jurisdiction to relieve against forfeiture of a proprietary (land, goods, shares or intellectual property: see 17.39) or possessory interest. But this jurisdiction does not provide relief from mere loss of personal contractual rights, such as the non-proprietary and non-possessory rights created under a licence.
- 17.30 *Nature of intermediate or innominate terms*. The question whether breach of an innominate or intermediate term justifies termination requires assessment of the consequences of breach. If those consequences are really severe (17.32), the innocent party can justifiably terminate. It will be seen immediately that this doctrine introduces, in favour of the guilty party, a more flexible approach, shielding him from the innocent party's over-zealous or punctilious demand for precise performance. The innominate term device is certainly an antidote to a ('draconian') regime of 'zero tolerance', where the innocent party can terminate a contract for technical and trivial breach, snapping at the slightest opportunity

108 M. Clarke, [1991] CLJ 29; G. H. Jones (with P. Schlechtriem), 'Breach of Contract', in *International Encyclopaedia of Comparative Law*, vol. VII, *Contracts in General* (Tübingen, 1999), 15-74, 15-190.

109 [1987] QB 527, 535-6, CA.

110 *United Scientific Holdings Ltd v. Burnley Borough Council* [1978] AC 904, HL; *Rainieri v. Miles* [1981] AC 1050, HL; *Union Eagle Ltd v. Golden Achievement Ltd* [1997] AC 514, PC; J. Stevens, (1998) 61 MLR 255 (on this last case, see 17.40).

111 *Bunge Corporation New York v. Tradax SA* [1981] 1 WLR 711, 715-16, 726, HL (also citing Lord Diplock in the *Photo Production* case, [1980] AC 822, 840, HL).

112 *British & Commonwealth Holdings plc v. Quadrex Holdings Inc.* [1989] QB 842, 857-9, CA, and *Behzadi v. Shaftesbury Hotels Ltd* [1992] Ch 1, 20, 26-7, 32, CA; further examined in *Re Olympia & York Canary Wharf Ltd (No. 2)* [1993] BCC 159; and other authorities are considered by *Chitty on Contracts* (30th edn, London, 2008), 21-014, 21-017.

to end the contract. But this antidote comes at a price. First, it can induce sloppiness in performance in commercial contexts. Secondly, it introduces considerable uncertainty in the application of contractual terms: assessment whether breach of an innominate term justifies termination can divide both arbitral panels and judges. Obtaining a final answer might require protracted and expensive litigation, and the decision might be taken on more than one appeal.

- 17.31 *Recognition of the ‘innominate term’ category in the Hongkong Fir case (1962).* In *Hongkong Fir Shipping Co. Ltd v. Kawasaki Kisen Kaisha Ltd* (1962),¹¹³ the concept of an innominate or intermediate term was recognised by the Court of Appeal (perhaps this was a judicial invention in 1962, although Lord Wilberforce in the *Schuler* case (1974)¹¹⁴ and Lord Denning in *The Hansa Nord* (1976)¹¹⁵ plausibly suggested that the broad notion of an innominate term in fact pre-existed this decision). In the *Hongkong Fir* case (1962), Diplock LJ rejected the contention that the law recognises only a simple dichotomy of promissory term consisting of ‘conditions’ and ‘warranties’, the latter producing only liability in damages, and the former entitling the innocent party additionally to terminate the contract.¹¹⁶ He accepted that some obligations can be breached only in a way which will necessarily have very serious consequences. Conversely, other contractual obligations might never have serious consequences, and so they should be regarded as ‘warranties’.¹¹⁷ But, as he emphasised, this leaves a large category of obligations ‘of a more complex nature’ where it will depend on the actual events following breach whether the innocent party can justify termination. (In 2007, the High Court of Australia in *Koompahtoo Local Aboriginal Land Council v. Sanpine Pty Ltd*¹¹⁸ acknowledged the threefold classification of conditions, intermediate terms and warranties, although Kirby J dissented, preferring to maintain a dichotomy of conditions and warranties, with a further rule that termination is justified, whether the obligation is a condition or warranty, if breach has deprived the innocent party of substantially the whole contractual benefit.)

- 17.32 *The Hongkong Fir case (1962) in detail.* In the *Hongkong Fir* case (1962),¹¹⁹ the Court of Appeal held that express terms as to seaworthiness should not be treated as conditions; and the court further held, agreeing with Salmon J at first instance, that termination was not justified for breach of innominate terms on these facts.

113 [1962] 2 QB 1, CA; D. Nolan, in C. Mitchell and P. Mitchell (eds.), *Landmark Cases in the Law of Contract* (Oxford, 2008), 269 ff; and, for Lord Diplock’s own account of this decision, see ‘The Law of Contract in the Eighties’ (1981) 15 *University of British Columbia Law Review* 371.

114 [1974] AC 235, 262F, HL: ‘I do not think this was anything new.’

115 *The Hansa Nord* [1976] 1 QB 44, 60, CA.

116 [1962] 2 QB 1, 69–70, CA.

117 *Ibid.*, at 70.

118 [2007] HCA 61; (2007) 82 ALJR 345, High Court of Australia (Glesson CJ, Gummow, Hedon and Crennan JJ; Kirby J dissenting) (noted by K. Dharmanda and A. Papamatheos, (2008) 124 LQR 373); for references to other common law jurisdictions on this topic, see A. Phang, ‘Doctrine and Fairness in the Law of Contract’ (2009) 29 LS 534, 546 ff.

119 [1962] 2 QB 1, CA.

The *Hongkong Fir* case concerned a two-year charterparty. Clause 1 required the ship to be 'in every way fitted for ordinary cargo service'. Clause 3 stipulated that the owners should maintain the ship in a 'thoroughly efficient state in hull and machinery during service'. But the *Hongkong Fir* was not 'shipshape and Bristol fashion': the chief engineer was addicted to drink, the crew was insufficient, and there were several serious breakdowns in the machinery. The charterers repudiated the agreement before the two-year period had elapsed. The owners alleged that there was no good reason for this. It was apparent that the charterers' motive in seeking to end the contract was that there had been a significant fall in the market rate for hire of such vessels, so that they were now locked into an uneconomic contract.¹²⁰

The Court of Appeal held that the express terms as to seaworthiness should not be treated as conditions, but instead as innominate terms; furthermore, termination was not justified on these facts. They noted that the 'seaworthiness' obligations could be breached in a variety of ways, some of them serious, others relatively minor. Diplock LJ regarded the terms as intermediate or innominate; Upjohn LJ, adopting a similar approach,¹²¹ agreed that, on the facts, the only remedy was damages rather than termination of the contract.¹²² The third judge, Sellers LJ, classified the term as a 'warranty'.¹²³

- 17.33** *Test for determining right to terminate for breach of an innominate or intermediate term.* Diplock LJ and the other judges in the *Hongkong Fir* case (1962) suggested that the true test is to consider whether the breach's effect has been to 'deprive the [innocent party] of substantially the whole benefit which it was the intention of the parties that he should obtain'.¹²⁴ This test is very generously weighted in favour of the party in breach. It is submitted that the Supreme Court might usefully re-open this question and that the test should be: 'Was the breach serious, as opposed to trivial or insignificant, in its impact?'
- 17.34** McKendrick collects a list of factors, emerging in later cases, which guide the conclusion whether to declare that termination is justified in this context:¹²⁵

[T]he losses caused by the breach, the cost of making performance comply with the terms of the contract, the value of the performance that has been received by the innocent party, the willingness of the party in breach to make good the consequences of the breach, the likelihood of a further breach by the party in breach, and the adequacy of damages as a remedy to the innocent party. Given the range of factors ... and their generality, the balancing of these factors must, at the end of the day, depend to a large extent upon the facts of the individual case.

¹²⁰ *Ibid.*, at 39 (Salmon J).

¹²¹ *Ibid.*, at 62.

¹²² *Ibid.*, at 64.

¹²³ *Ibid.*, at 60.

¹²⁴ *Ibid.*, at 69–70 (similarly, *ibid.*, at 57 and 64, *per* Sellers and Upjohn LJ).

¹²⁵ E. McKendrick, *Contract Law: Text, Cases and Materials* (4th edn, Oxford, 2010), 783; for a similar list, see *Restatement of the Law Second, Contracts*, section 241, on which see G. H. Jones (with P. Schlechtriem), 'Breach of Contract', in *International Encyclopaedia of Comparative Law*, vol. VII, *Contracts in General* (Tübingen, 1999), 15–131.

- 17.35 *Statutory control in commercial sales upon 'over-technical' resort to termination.* In the context of sales of goods (and goods and services transactions),¹²⁶ a 1994 statutory amendment, section 15A of the Sale of Goods Act 1979, is designed to counter over-technical (for examples, see 17.36) termination by *commercial* buyers based on sellers' breaches of implied conditions. The change had been recommended by the Law Commission (1987).¹²⁷ But Treitel was unimpressed, commenting that 'the section undermines the certainty which classification of the implied terms in question as conditions was intended to provide'.¹²⁸
- 17.36 Section 15A¹²⁹ of the Sale of Goods Act 1979 allows the courts to hold that a buyer cannot reject goods even though the seller has breached one of the implied terms contained in sections 13–15 of that Act (all of those provisions insert implied terms which are classified as *conditions*). This result is expressed as follows: '[T]he breach is not to be treated as a breach of condition but may be treated as a breach of warranty.' Section 13(1) concerns correspondence of goods with their description, whether or not the sale is made by a seller in the course of business. Section 14(2) imposes the requirement that goods sold by a seller in the course of business must be 'of satisfactory quality'. Section 14(3) imposes the requirement that goods sold by a seller in the course of business are 'reasonably fit for' any 'particular purpose'. This possibility arises if the buyer 'expressly or by implication makes known to the seller any particular purpose for which the goods are being bought'. Section 15(2) concerns correspondence to sample, and imposes the further requirement that the goods must be 'free from any defect making their quality unsatisfactory' if this defect 'would not be apparent on reasonable examination of the sample'. Under the new regime of section 15A, a commercial buyer will be entitled only to damages, and will not be entitled also to terminate the contract, if (i) the breach is so 'slight' that it would be 'unreasonable' to reject the goods; (ii) both the parties are engaged in trade or business; and (iii) the contract neither expressly nor impliedly precludes this conclusion.¹³⁰ The seller bears the burden of proving (i).¹³¹ The test stated at (i) is an objective inquiry: there is no need to prove subjective bad faith on the buyer's part. The same provision states that it will not apply if 'a contrary intention appears in, or is to be implied from, the contract'.¹³² And so this set of provisions will *not* affect the situation where the parties have *expressly categorised a term as a condition*, thereby permitting termination, no matter how slight the breach, or where the parties have expressly stated that termination is justified no matter how slight the defective performance might be. It should be noted that section 15A does not render the seller's obligation an intermediate term in the common law sense. Instead, section 15A permits the commercial buyer to terminate unless the breach is 'slight'. If the breach is not slight, the *second* issue of reasonableness does not

126 Parallel provisions appear in sections 5A and 10A of the Supply of Goods and Services Act 1982.

127 Amendment made in 1994, implementing the recommendations of the Law Commission: see Law Commission, *Sale and Supply of Goods* (Law Commission Report No. 160, Cm 137, London, 1987).

128 Treitel (12th edn, London, 2007), 18-054.

129 For details, see *Benjamin's Sale of Goods* (7th edn, London, 2006), 12.024 ff.

130 On this last factor, see section 15A(2) of the Sale of Goods Act 1979.

131 *Ibid.*, section 15A(3).

132 *Ibid.*, section 15A(2).

arise. By contrast, breach of an intermediate term justifies termination only if the innocent party is substantially deprived of the expected benefit (17.33). Section 15A adopts a different emphasis, therefore. In 2006, *Benjamin* noted that there has been no reported case on this provision,¹³³ and none is recorded since. There is a parallel provision: section 30(2A) of the 1979 Act adopts a similar approach where goods delivered to a non-consumer are less than, or greater than, the quantity contracted for, but this quantitative deviation is 'so slight that it would be unreasonable' for the buyer to reject the goods.

Section 15A and two older cases. Section 15A of the Sale of Goods Act 1979 (17.35) is intended to prevent over-technical resort by buyers of sellers' breaches of conditions. For example, in *Re Moore & Co. and Landauer & Co.* (1921),¹³⁴ the buyer was held to be entitled to reject goods (some of which were) sent in boxes of twenty-four rather than in boxes of thirty, the contract having required boxing in quantities of thirty. The assumption made here is that the contractual description of the goods' packaging would form part of the implied term concerning a sale by description under section 13(1) of the Sale of Goods Act 1979. In this case, Scrutton LJ (a celebrated authority on commercial law) said (Bankes and Atkin LJJ agreeing):¹³⁵

[A] man who has bought under a contract thirty tins to the case may have sold under the same description, and may be placed in considerable difficulty by having goods tendered to him which do not comply with the description under which he bought, or under which he has resold.

Such facts would now be subject to the twofold test of section 15A: (i) was the breach of condition in fact so 'slight' that (ii) it would be 'unreasonable' for the buyer to reject? It seems highly probable that this test would now operate in favour of the seller in such a case.

However, deviations in 'throw away packaging' are one thing. Failure to supply goods corresponding to the stipulated dimensions might not be so easily tolerated under the new regime of section 15A. Thus, Treitel queries whether this new provision would make a difference on the facts of *Arcos v. Ronaasen* (1933) where the supply of timber of 9/16ths of an inch was held not to be equivalent to the contractually stipulated dimension of half an inch (8/16ths).¹³⁶

In the *Arcos* case (1933), the buyer undertook to supply timber 'half an inch' thick. But the timber had swollen following exposure to damp. When delivered, the timber was 9/16ths of an inch thick. At trial and on successive appeals, it was unanimously held that the seller was in breach of an implied condition that the goods would correspond to their 'description' (now section 13(1) of the Sale of Goods Act 1979). In the House of Lords, Lord Atkin emphasised

¹³³ For details, see *Benjamin's Sale of Goods* (7th edn, London, 2006), 12.024 ff.

¹³⁴ [1921] 2 KB 519, CA.

¹³⁵ *Ibid.*, at 524.

¹³⁶ [1933] AC 470, HL.

that the goods did not conform to the contractual description. That breach of a condition entitled the buyer to reject.

Lord Atkin suggested that if the seller had wanted to bargain for a 'margin of tolerance', it might have expressly stipulated for this. This was not, he added, a 'microscopic' deviation from a contractual specification. It was irrelevant that the buyer's true motive in rejecting the goods was to escape a bargain. The price had become unattractive because the market price of timber had fallen between the date of contract and that of delivery. But the law does not scrutinise and weigh the buyer's motives.¹³⁷ Finally, Lord Atkin added that it was not a sound counter-argument for the seller to assert that the goods were fit for their intended purpose (now section 14(3) of the 1979 Act). It was true that the buyer might have used the wood for its intended purpose, which was for use in the construction of cement barrels. But he suggested that this was a bad point because a buyer might legitimately change his intentions and wish to use the goods for another purpose. If so, the fact that the goods did not correspond with their contractual description might render them unsuitable for that new purpose.

In light of the new section 15A, Treitel comments on these facts that the difference between half an inch and 9/16ths is not necessarily 'slight', as required by that provision.¹³⁸ If so, the second issue of reasonableness does not arise for consideration. If Treitel is correct, the buyer could still justifiably terminate the contract, even after enactment of section 15A.

- 17.37 *Sale of goods transactions and intermediate terms.* In '*The Hansa Nord*' (1976), the Court of Appeal held that an agreement falling within the scope of the sale-of-goods legislation (then the 1893 Act, now the 1979 Act) might contain an intermediate term even though the statute (in its classification of promissory terms) does not include that expression and instead refers to the simple dichotomy of conditions and warranties.¹³⁹

The contract in '*The Hansa Nord*' (1976) concerned the supply of citrus pulp pellets at Rotterdam. These were to be used to manufacture cattle-feed. It was an express term that they should be delivered in good condition. The buyer rejected them when he discovered that some of the cargo was less than perfect (the market price had fallen so that this had become a bad bargain for the buyer). The seller then resold the goods at auction to an importer, X. The buyer (who had just pulled out from the original deal) later bought these goods from the third party, X, for a much smaller sum than he had originally agreed to pay the original vendor (£33,720 rather than £100,000). It appears that the product had not deteriorated to the point that it could not be used lawfully and successfully to produce cattle-feed. The seller contended

137 E. McKendrick, *Contract Law: Text, Cases and Materials* (4th edn, Oxford, 2010), 787–8, reviews proposals for taking account of such motives: see also R. Brownsword, (1992) 5 *Journal of Contract Law* 83, 91–3.

138 Treitel (12th edn, London, 2007), 18-054.

139 '*The Hansa Nord*' [1976] QB 44, CA, noted by A. Weir, [1976] CLJ 33.

successfully that the buyer had not been entitled to reject the goods, and therefore the buyer should be confined to a claim for damages.

The Court of Appeal classified the present obligation as an intermediate term, rather than an express condition. It also held that there had been no breach of the (then applicable) statutory implied term that the goods must be of 'merchantable quality' on the present facts.¹⁴⁰ So the court revoked the arbitrator's order for repayment of the price, and instead remitted the case for assessment of damages, based on the difference in the value of the goods supplied and of sound goods.

Roskill and Ormrod LJ noted that the sale-of-goods legislation (now section 62(2) of the 1979 Act) requires the 'rules of the common law' to apply to sale-of-goods transactions.¹⁴¹ One of these common law rules is the rule which was stated (or perhaps 'rediscovered') in the *Hongkong Fir* case (1962) (17.31): that a contractual obligation might be 'intermediate' or 'innominate'; if so, the innocent party's capacity to terminate the contract will depend on the gravity or otherwise of the breach, having regard to the actual consequences of that breach.

- 17.38** *Repetitive breach in continuing contracts.* In continuing contracts, a party's *repeated breaches* might justify the other in terminating the contract even though there has been neither a breach of a 'condition', nor a clear communication of unwillingness to honour the contract. The court will assess whether the other side's default is grave enough, presently and prospectively, so as to strike at the root of the other party's contractual expectations. In *Rice v. Great Yarmouth Borough Council* (2000),¹⁴² Hale LJ said that the test is whether the innocent party 'would thereby be deprived of a substantial part of that which it had contracted for that year, subject to the additional possibility that some aspects of the contract were so important that the parties are to be taken to have intended that depriving [the innocent party] of that part of the contract would be sufficient in itself. On the facts of the *Rice* case (17.25), the Court of Appeal affirmed the trial judge's decision, that the defendant contractor's successive failures to maintain the claimant's parks were not serious enough to satisfy this test.

5. RELIEF AGAINST FORFEITURE OF PROPRIETARY OR POSSESSORY INTERESTS¹⁴³

- 17.39** This is another possible fetter upon an innocent party's capacity to call off a deal on the basis of the other party's contractual default. The main contexts in which this jurisdiction

¹⁴⁰ *Ibid.*, at 61–3, 77, 79, CA, considering section 14(2) of the Sale of Goods Act 1893; now section 14(2) of the 1979 Act, which is concerned with the implied term that goods be of 'satisfactory quality', as amplified by section 14(2A) to (2F)).

¹⁴¹ *Ibid.*, at 72, 83, CA.

¹⁴² *The Times*, 26 July 2000; (2001) 3 LGLR 4, CA, at [38].

¹⁴³ Robert Walker LJ in *On Demand plc v. Gerson plc* [2001] 1 WLR 155, 163G–172, CA (reversed on another basis at [2003] 1 AC 368, HL), noting a long line of cases; L. Gullifer, in A. Burrows and E. Peel

operates are relief in favour of borrowers or tenants for non-payment of mortgage debts or of rent. This jurisdiction cannot be employed as a means of rewriting an unfavourable bargain.¹⁴⁴ Nor can it be applied when it is too late to seek relief because the subject matter of a lease has already been sold to a third party. In such a case, it will not be possible to restore the parties to the *status quo*.¹⁴⁵ The jurisdiction is not confined to land, but can include chattels, and intangible property, such as shares or proprietary interests in intellectual property rights. It does not apply to mere *in personam* rights, that is, rights in another's property held by a mere *licensee*, incapable of being asserted against third parties, but creating merely an obligation and right as between licensor and licensee.¹⁴⁶ Equitable relief is confined to 'proprietary or possessory interests'. The House of Lords in the *Sport International* case (1984) drew a distinction between mere contractual rights (such as a licensee's right to intellectual property) and enjoyment of a 'proprietary' or 'possessory' interest.¹⁴⁷ Thus, a licensee's rights under a trade mark agreement are neither possessory nor proprietary for this purpose.¹⁴⁸ Nor, as decided in '*The Scraptrade*' (1983), is a 'time charterparty' a proprietary or possessory interest.¹⁴⁹ Money does not¹⁵⁰ fall within this doctrine's scope, unless it takes the form of a proprietary interest, as under a trust, or a beneficial interest in a resulting or constructive trust¹⁵¹ (otherwise, forfeiture of money payments is subject to relief in the case of deposits or instalment payments, according to the doctrine in *Stockloser v. Johnson* (1954): see 19.27 and 19.25).

- 17.40 The Privy Council in *Union Eagle Ltd v. Golden Achievement Ltd* (1997) held that relief against forfeiture of a proprietary or possessory interest does not protect a purchaser of real property who has yet to go into possession of the relevant property.¹⁵² Otherwise, unacceptable uncertainty would arise. Vendors would lose 'bright line' protection of the strict common law rights. Those rights enable them to walk away from the deal with the purchaser if he is late in paying the purchase money.

The *Union Eagle* case (1997) concerned the purchase of a flat in Hong Kong. The purchaser's tender of the price was ten minutes late. On a rising market, the vendor decided to

(eds.), *Commercial Remedies: Current Issues and Problems* (Oxford, 2003), 191, at 212 ff; M. Tilbury, in P. Parkinson (ed.), *Principles of Equity* (Sydney, 1996), chapter 9; *Meagher, Gummow and Lehane's Equity: Doctrines and Remedies* (4th edn, Sydney, 2003), 18-025 to 18-075.

144 Robert Walker LJ in *On Demand* case, [2001] 1 WLR 155, 163G-172, CA (reversed on another basis at [2003] 1 AC 368, HL).

145 *Ibid.*

146 *Sport Internationals Bussum BV v. Inter-Footwear Ltd* [1984] 1 WLR 776, HL (considered in *Celestial Aviation 1 Ltd v. Paramount Airways Private Ltd* [2010] EWHC 185 (Comm); [2010] 1 CLC 15, Hamblen J; noted by L. Aitken, (2010) 126 LQR 505-7; see also *UK Housing Alliance (North West) Ltd v. Francis* [2010] EWCA Civ 117; [2010] 3 All ER 519, at [14]; noted by C. Conte, (2010) 126 LQR 529-34).

147 *Sport Internationals Bussum BV v. Inter-Footwear Ltd* [1984] 1 WLR 776, 794, HL.

148 *Ibid.*

149 [1983] 2 AC 694, HL.

150 *UK Housing Alliance (North West) Ltd v. Francis* [2010] EWCA Civ 117; [2010] 3 All ER 519, at [14], *per* Longmore LJ (loss of contingent right to a payment; noted by C. Conte, (2010) 126 LQR 529-34).

151 *Nutting v. Baldwin* [1995] 1 WLR 201, 209, *per* Rattee J.

152 [1997] AC 514, PC.

terminate the contract and forfeit the deposit. The purchaser's argument was that equity could provide discretionary relief from the vendor's decision not to proceed with the sale. This argument was based on the purchaser's acquisition of a constructive trust interest, that is, an inchoate equitable title to the property. That interest had arisen before the buyer defaulted by making late payment of the price. This equitable interest, according to the purchaser, had been forfeited summarily by the vendor's decision to seize upon the purchaser's ten-minute delay as a ground for terminating the contract and triggering forfeiture of the deposit.

But this argument was rejected. The Privy Council held that equity's intervention in this context would over-complicate the contractual termination of transactions where timely payment has clearly been made 'of the essence'. Lord Hoffmann, giving the Privy Council's judgment, held that unacceptable uncertainty would arise. Vendors would lose 'bright line' protection of their strict common law rights. They should be free to walk away from the deal if the purchase money is paid late when punctual performance 'is of the essence'. It is difficult to quarrel with this vote in favour of certainty. Lord Hoffmann explained:¹⁵³ 'the right to [terminate the contract for breach], though it involves termination of the purchaser's equitable interest, [has as its] purpose [the need to] restore to the vendor his freedom to deal with his land as he pleases ... [A] vendor should be able to know with reasonable certainty whether he may resell the land or not'.

6. THE PROCESS OF TERMINATION FOR BREACH

- 17.41 *Innocent party's choice*. Faced by the other party's repudiation (anticipatory breach, or renunciation at time of due performance, or other breach which justifies termination), the innocent party has a choice: he can accept the repudiation and thus terminate the contract and sue for damages, or he can affirm the contract and sue for damages.¹⁵⁴ This is known as 'the right to elect'. After some doubt, the same analysis applies where there has been attempted repudiation of an employment contract by an employer.¹⁵⁵

There is an exception to this 'elective' or non-automatic termination analysis in the context of insurance contracts. Important clauses are there known curiously as 'warranties'. In that context, the contract automatically terminates if such a term is breached. And so an insurer is not bound to make an indemnity payment if the insured transgresses or fails to satisfy one of these warranties.¹⁵⁶

¹⁵³ *Ibid.*, at 520.

¹⁵⁴ *Ferrometal SARL v. Mediterranean Shipping Co. SA ('The Simona')* [1989] AC 788, HL; *Vitol SA v. Norelf Ltd ('The Santa Clara')* [1996] AC 800, HL.

¹⁵⁵ *Soares v. Beazer Investments Ltd* [2004] EWCA Civ 482 (porter remaining in occupation of flat and in receipt of wages after purported repudiation by employer); tangle of earlier cases noted: *Boyo v. Lambeth London Borough Council* [1994] ICR 727 (considering *London Transport Executive v. Clarke* [1981] ICR 355, CA; *Gunton v. Richmond upon Thames London Borough Council* [1981] Ch 448, CA).

¹⁵⁶ *Bank of Nova Scotia v. Hellenic Mutual War Risk Association (Bermuda) Ltd ('The Good Luck')* [1992] 1 AC 233, HL; Treitel, *Some Landmarks of Twentieth Century Contract Law* (Oxford, 2002), 127.

- 17.42 *Binding nature of the election.* The law requires firm adherence to the innocent party's decision to terminate or to affirm the contract. Once a decision to terminate has been communicated, it is too late to try to resurrect the contract.¹⁵⁷ Similarly, once the innocent party decides to affirm the contract, he cannot change his mind, at least where he has full knowledge¹⁵⁸ of the relevant facts and of his right to terminate. Lord Goff in *'The Kanchenjunga'* (1990) suggested that the innocent party might be estopped from terminating because his conduct has caused the other party to change his position.¹⁵⁹ A party can also waive a breach of condition (see the first phase of default in the *Schuler* case 1974, chronicled at 17.20), or, in the case of sales of goods, a buyer can be treated under statutory rules as having 'accepted' the goods.¹⁶⁰
- 17.43 *No third choice.* The innocent party has no 'third' choice. He cannot 'affirm the contract and yet be absolved from tendering further performance unless and until [the repudiating party] gives reasonable notice that he is once again able and willing to perform'.¹⁶¹ In other words, once the innocent party decides to continue with the contract, he too is 'back on track' and must comply with his contractual obligations as they remain or arise. As Lord Ackner explained in *'The Simona'* (1989):¹⁶²

There is no third choice, as a sort of *via media*, to affirm the contract and yet to be absolved from tendering further performance unless and until A gives reasonable notice that he is once again able and willing to perform ... [This is because] such a [third] choice would negate the contract being kept alive for the benefit of both parties and would deny the party [party A] who [attempted to repudiate], the right to take advantage of any supervening circumstance which would justify him in declining to complete.¹⁶³

This decision, in the words of Lord Mustill,¹⁶⁴ ended the debate engendered by 'a notorious trio of cases'¹⁶⁵ which had 'caused generations of contract lawyers to quail'.

157 *Yukong Line of Korea v. Rendsburg Investments Corporation of Liberia* [1996] 2 Lloyd's Rep 604, Moore-Bick J, proposition (4).

158 *Peyman v. Lanjani* [1985] Ch 457, CA.

159 [1990] 1 Lloyd's Rep 391, 399, HL, *per* Lord Goff; for other common law discussion, see G. H. Jones (with P. Schlechtriem), 'Breach of Contract', in *International Encyclopaedia of Comparative Law*, vol. VII, *Contracts in General* (Tübingen, 1999), 15-134, 15-135.

160 For 'acceptance' in the context of sales of goods, see sections 11(4), 35, 35A and 36 of the Sale of Goods Act 1979; *Anson's Law of Contract* (29th edn, Oxford, 2010), 150-5.

161 *Fercometal SARL v. Mediterranean Shipping Co. SA ('The Simona')* [1989] AC 788, 805E, HL, *per* Lord Ackner (criticised by G. H. Jones and W. Goodhart, *Specific Performance* (2nd edn, London, 1996), 69-72, considering the Australian cases of *Foran v. Wight* (1989) 168 CLR 385 (High Court of Australia), and *Peter Turnbull & Co. v. Mundus Trading Co. (Australasia)* (1954) 90 CLR 235, High Court of Australia); M. Mustill, *Anticipatory Breach: Butterworths Lectures 1989-90* (London, 1990), 65-8 and J. Carter, in J. Beatson and D. Friedmann (eds.), *Good Faith and Fault in Contract Law* (Oxford, 1995), 485, 498, 502-4.

162 *Fercometal SARL v. Mediterranean Shipping Co. SA ('The Simona')* [1989] AC 788, 805E-F, HL.

163 *Ibid.*

164 M. Mustill, *Anticipatory Breach: Butterworths Lectures 1989-90* (London, 1990), 65.

165 *Braithwaite v. Foreign Hardwood Co.* [1905] 2 KB 543, CA; *Taylor v. Oakes Roncoroni & Co.* (1922) 27 Com Case 261, 268, CA; *British & Benningtons v. North West Cachart Co.* [1923] AC 48, HL; Lord Ackner dealt with the first two decisions in the *Fercometal* case at [1989] AC 788, 801-5.

- 17.44 *Innocent party's pause for thought.* However, according to Rix LJ in the *Stocznia* case (2003), this last point in '*The Simona*' case should not be taken too far: it *does not prevent* the courts from recognising the innocent party's need to pause for thought. Rix LJ held that there is an obvious practical need to allow the innocent party a reasonable opportunity to assess briefly his option whether to affirm or to terminate, just as in international rugby the fourth official can be given a reasonable time to study camera footage to determine whether a disputed try should be awarded or not. But the time for assessment should not be prolonged. As Rix LJ said:¹⁶⁶ 'If he does nothing for too long, there may come a time when the law will treat him as having affirmed.'
- 17.45 *New opportunity to terminate.* A party might gain a fresh right to elect to terminate the contract, because the other party commits a fresh repudiation,¹⁶⁷ or because the guilty party's breach is continuous, such as a failure to pay money.¹⁶⁸ As Rix LJ said, also in the *Stocznia* case (2003):¹⁶⁹ 'If [the innocent party] maintains the contract in being for the moment, while reserving his right to treat it as repudiated if his contractual party persists in his repudiation, then he has not yet elected.'
- 17.46 *Equivocal exercise of the right to terminate the contract.* The innocent party's decision whether to affirm or to terminate the contract requires no particular form. It can be manifested expressly or impliedly (see also 17.47).¹⁷⁰
- 17.47 *A decision to terminate effected by conduct or silence.* But can such a decision be inferred from conduct or silence? The answers are: from conduct, certainly; from silence, occasionally, but only if the inference can be safely drawn from the relevant context. These points will now be elaborated.

The House of Lords in *Vitol SA v. Norelf Ltd* (1996) held that *conduct* can be effective to communicate a decision to terminate the contract:

An act of acceptance of a repudiation requires no particular form: a communication does not have to be couched in the language of acceptance. It is sufficient that the communication or conduct clearly and unequivocally conveys to the repudiating party that that aggrieved party is treating the contract as at an end.¹⁷¹

As for *silence* or an *omission to act*, Lord Steyn said:¹⁷²

166 *Stocznia Gdanska SA v. Latvian Shipping Co. (No. 3)* [2002] EWCA Civ 889; [2002] 2 All ER (Comm) 768, at [87].

167 *Yukong Line of Korea v. Rendsburg Investments Corporation of Liberia* [1996] 2 Lloyd's Rep 604, Moore-Bick J, proposition (5).

168 *Stocznia* case, [2002] EWCA Civ 889; [2002] 2 All ER (Comm) 768, at [96] to [100].

169 *Ibid.*, at [87].

170 *Vitol SA v. Norelf Ltd ('The Santa Clara')* [1996] AC 800, 810–11, HL, *per* Lord Steyn; *Yukong Line of Korea v. Rendsburg Investments Corporation of Liberia* [1996] 2 Lloyd's Rep 604, Moore-Bick J, proposition (7).

171 *Vitol SA v. Norelf Ltd ('The Santa Clara')* [1996] AC 800, 810–11, *per* Lord Steyn, noted by S. Hedley, [1996] CLJ 430–2.

172 *Ibid.*, at 811, *per* Lord Steyn.

I am satisfied that a failure to perform may sometimes signify to a repudiating party an election by the aggrieved party to treat the contract as at an end. Postulate the case where an employer at the end of a day tells a contractor that he, the employer, is repudiating the contract and that the contractor need not return the next day. The contractor does not return the next day or at all. It seems to me that the contractor's failure to return may, in the absence of any other explanation, convey a decision to treat the contract as at an end.

7. TERMINATION FOR BREACH AND RESCISSION FOR MISREPRESENTATION ETC. CONTRASTED

- 17.48 Modern decisions distinguish two processes of terminating a contract, depending on whether (1) the ground of termination is an initial impediment to the contract (the contract being 'vitiated', for example, for misrepresentation or duress); and (2) whether, by contrast, the contract's life is cut short, before complete performance, by supervening impossibility or frustration (17.50) or because an innocent party has chosen to *terminate the contract for breach*. As for (1), 'rescission' (9.18 ff) involves the contract being dismantled with retro-active effect, with a mutual restoration of benefits. As for (2), such termination brings the contract to an end from that point in time, but only prospectively. It does not annihilate the contract retrospectively. This is, therefore, prospective termination or termination *in futuro* (see also 9.22 to 9.25). It follows that the innocent party retains the right to sue in respect of preceding breaches.¹⁷³ Similarly, termination for breach does not disturb accrued obligations to pay agreed sums, for example, a partner's liability to make contributions to partnership expenses¹⁷⁴ or liability to pay accrued instalments under contract for construction of a ship.¹⁷⁵ Furthermore, various ancillary obligations will continue to apply, notably: exclusion clauses;¹⁷⁶ liquidated damages clauses; choice-of-law clauses (9.25, and especially 12.05);¹⁷⁷ jurisdiction clauses (12.07);¹⁷⁸ arbitration clauses (12.09 ff);¹⁷⁹

173 *Photo Production Ltd v. Securicor Transport Ltd* [1980] AC 827, 849, HL, *per* Lord Diplock; other leading authorities: *McDonald v. Dennys Lascelles Ltd* (1933) 48 CLR 457, 476–7, High Court of Australia, Dixon J; *Heyman v. Darwins Ltd* [1942] AC 356, 397, HL, Lord Porter; *Lep Air Services Ltd v. Rolloswin Investments Ltd* [1973] AC 331, 349–51, HL, Lord Diplock; *Johnson v. Agnew* [1980] AC 367, 396, HL, Lord Wilberforce; *Bank of Boston Connecticut v. European Grain and Shipping Ltd* [1989] AC 1056, 1098–9, HL, *per* Lord Brandon; *Stocznia Gdanska SA v. Latvian Shipping Co.* [1998] 1 WLR 574, HL; *Hurst v. Bryk* [2002] 1 AC 185, HL. On *Johnson v. Agnew*, see the study by C. Mitchell, in C. Mitchell and P. Mitchell (eds.), *Landmark Cases in the Law of Contract* (Oxford, 2008), 351 ff.

174 *Hurst v. Bryk* [2002] 1 AC 185, HL.

175 *Stocznia Gdanska SA v. Latvian SS Co.* [1998] 1 WLR 574, HL, noted by J. Beatson and G. Tolhurst, [1998] CLJ 253.

176 *Photo Production Ltd v. Securicor Transport Ltd* [1980] AC 827, HL.

177 This follows a *fortiori* from *Mackender v. Feldia AG* [1967] 2 QB 590, CA (rescission for non-disclosure under an insurance contract *does not wipe out* (1) a jurisdiction and (2) a choice-of-law clause: see especially, Diplock LJ at 603–4); J. Carter, in M. Furmston (ed.), *The Law of Contract* (3rd edn, London, 2007), 7.40.

178 See *Mackender v. Feldia AG* [1967] 2 QB 590, CA; note also the *general reasoning* of Lord Wilberforce in *Port Jackson Stevedoring Pty v. Salmond & Spraggon (Australia) Pty ('The New York Star')* [1981] 1 WLR 138, 145, PC.

179 *Heyman v. Darwins Ltd* [1942] AC 356, 374, HL; see also the next note.

a consensual time bar;¹⁸⁰ and a stipulation for a retainer in an agency contract.¹⁸¹ Finally, a clause allowing for inspection of documents was held to have survived after an agency agreement was terminated for breach in the *Yasuda Fire* case (1995).¹⁸²

However, according to the House of Lords decision in *General Billposting Co. Ltd v. Atkinson* (1909), restrictive covenants (inserted into partnership or employment contracts) do not survive in favour of the guilty party.¹⁸³ One set of commentators has suggested that this is an elementary matter of 'common sense', presumably on the basis that the repudiation disentitles the guilty party from taking advantage of such a constraining provision.¹⁸⁴ But, in *Campbell v. Frisbee* (2002),¹⁸⁵ Lord Phillips MR sceptically commented on the *General Billposting* case (1909), noting his earlier remarks in a different case:

[In] *Rock Refrigeration Ltd v. Jones* (1997)¹⁸⁶ ... the majority proceeded on the basis that *General Billposting Co. Ltd v. Atkinson* (1909) remained good law. Phillips LJ [later Lord Phillips MR] questioned, however, whether the principle underlying it could survive the development of contract law exemplified by *Photo Production Ltd v. Securicor Transport Ltd*.¹⁸⁷

In an appeal from a summary judgment, the Court of Appeal in *Campbell v. Frisbee* (2002) declared that the position regarding confidentiality clauses is developing, and the court decided to leave the matter open: 'We do not believe that the effect on duties of confidence assumed under contract when the contract in question is wrongfully repudiated is clearly established.'¹⁸⁸

The 'prospective' operation of termination for breach accords with the (non-binding) *Principles of European Contract Law*, Article 9:305(1), and with UNIDROIT's *Principles of International Commercial Contracts* (2004), Article 7.3.5.¹⁸⁹ In particular, both acknowledge (Article 9:305(1) of PECL; Article 7.3.5(3) of UNIDROIT) specifically that 'a provision for the settlement of disputes' survives that form of termination, as well as (as it is put vaguely) 'any other term of the contract/provision which is to operate even after termination'.

It should also be noted that, in an instalment contract, A might repudiate only *vis-à-vis* a severable part of the contract, justifying termination by B of that part, but not

180 *Port Jackson Stevedoring Pty v. Salmond & Spraggon (Australia) Pty* ('The New York Star') [1981] 1 WLR 138, 145, PC, *per* Lord Wilberforce.

181 *Duffen v. FRA BO Spa (No. 2)* [2000] 1 Lloyd's Rep 180 (Judge Hallgarten QC, Central County Court, London).

182 *Yasuda Fire & Marine Insurance Co. of Europe Ltd v. Orion Marine Insurance Underwriting Agency Ltd* [1995] QB 174, Colman J.

183 [1909] AC 118, HL.

184 M. Furmston (ed.), *The Law of Contract* (3rd edn, London, 2007), 5.112.

185 [2002] EWCA Civ 1374; [2003] ICR 141, at [22].

186 *Rock Refrigeration Ltd v. Jones* [1997] ICR 938, 959–60, CA; J. Carter, in M. Furmston (ed.), *The Law of Contract* (3rd edn, London, 2007), 7.40.

187 [1980] AC 827, HL; *Hurst v. Bryk* [2002] 1 AC 185, HL.

188 [2002] EWCA Civ 1374; [2003] ICR 141, at [22].

189 2nd edn, Rome, 2004; see M. J. Bonell (ed.), *The UNIDROIT Principles in Practice: Case Law and Bibliography on the UNIDROIT Principles of International Commercial Contracts* (2nd edn, Ardsley, NY, 2006), 387; S. Vogenauer and J. Kleinheisterkamp (eds.), *Commentary on the UNIDROIT Principles of International Commercial Contracts* (Oxford, 2009), 854 ff.

justifying termination of the whole contract. Mance LJ noted this possibility in *Friends Provident Life & Pensions Ltd v. Sirius International Insurance Corp.* (2005): '[A] failure under a contract for sale by instalments to make due delivery of one instalment within the contractually stipulated time may be accepted as repudiatory of that instalment, but does not necessarily mean that the whole contract comes to an end.'¹⁹⁰

- 17.49 In view of the modern analytical distinction between rescission for misrepresentation (or some other preliminary ground of vitiation) and termination for breach (on this distinction, see 17.48), the term 'rescission' is best confined to the process of setting aside retrospectively a contract which is vitiated by reason of misrepresentation, or other grounds of initial invalidity.

As Lord Wilberforce explained in *Johnson v. Agnew* (1980):¹⁹¹

[A]lthough the [innocent party] is sometimes referred to in the above situation as 'rescinding' the contract, this so-called 'rescission' is quite different from rescission *ab initio*, such as may arise for example in cases of mistake, fraud or lack of consent.

He continued:

In those cases [of rescission *ab initio*], the contract is treated in law as never having come into existence ... In the case of an accepted repudiatory breach, the contract has come into existence but has been put an end to or discharged.

He concluded:

[I]t is now quite clear, under the general law of contract, that acceptance of a repudiatory breach does not bring about 'rescission *ab initio*'.

In *Hurst v. Bryk* (2002), Lord Millett said that 'failure to distinguish between discharge for breach and rescission *ab initio* has led many courts astray and continues to do so.'¹⁹²

Most commentators recognise the need for terminological precision and have abandoned the old ambiguous language of 'rescission for breach'. However, as recently as 2003, *Treitel* adhered to the phrase 'rescission for breach'.¹⁹³ But this terminology has been abandoned by the new editor of *Treitel*.¹⁹⁴

- 17.50 Frustration also causes the contract to end prospectively, so that at common law accrued obligations to pay or perform remain exigible (on the impact of the Law Reform (Frustrated Contracts) Act 1943, see 16.21 ff). Here, it is enough to note that termination for frustration operates automatically ('by operation of law') and is not

190 [2005] EWCA Civ 601; [2005] 2 Lloyd's Rep 517, at [31].

191 [1980] AC 367, 392–3, HL.

192 [2002] 1 AC 185, 194, HL.

193 In the last edition (11th edn, London, 2003) to be edited by Treitel, at 760 (but see the next note).

194 Edwin Peel, editor of *Treitel* (12th edn, London, 2007), chapters 17, 18, preferring instead the expression 'termination for breach'.

dependent on any election by either party. Indeed, many instances of frustration occur without the parties (or their successors) being aware that the Angel of Death has passed over their contract.

8. THE ENTIRE OBLIGATION RULE¹⁹⁵

17.51 In contracts for services, or for goods and services, payment might be expressly or impliedly postponed until the job is completed. The ‘entire obligation’ rule will then prevent the contractor from becoming entitled to payment until conclusion of the job. For example, in contracts between householders and jobbing builders, the consumer normally postpones payment until the whole job is done (only a fool, although they exist, would pay a builder or decorator by the hour or by the day: but nearly all litigants are fools, because their lawyers are usually paid by the six-minute ‘unit’). As Brian Davenport QC observed in a Law Commission report in 1983: ‘Experience has shown that it is all too common for such builders not to complete one job before moving on to the next.’¹⁹⁶ The entire obligation rule also reduces litigation, because it confers a self-help defensive remedy (a shield) upon the innocent party. The latter is spared the inconvenience, delay, expense and anxiety of seeking damages for the cost of curing a defective job in the courts.

17.52 At common law, it made no difference whether the failure to complete the contractual obligation involved breach or frustration. In *Cutter v. Powell* (1795),¹⁹⁷ P hired C as a second mate for a voyage from Jamaica to Liverpool at a rate significantly higher than the local rate. Before the ship had reached Liverpool, C died and his widow sued for wages. The claim failed because payment required completion of the trip, and it did not matter whether C had jumped ship, been killed on board or died of natural causes (although if he had been pressganged by the King’s officers into working on a naval ship, the seaman would have been entitled to a proportionate part).¹⁹⁸ Lord Kenyon said:¹⁹⁹

Here the defendant expressly promised to pay the [sailor] thirty guineas, provided he proceeded, continued and did his duty as second mate in the ship from Jamaica to Liverpool ... [I]f there had been no contract between these parties, all that the [sailor] could have recovered on a *quantum meruit* for the voyage would have been eight pounds ... [The sailor] stipulated to receive the larger sum if the whole duty were performed, and nothing unless the whole of that duty were performed: it was a kind of insurance.

195 B. McFarlane and R. Stevens, (2002) 118 LQR 569; G. H. Jones (with P. Schlechtriem), ‘Breach of Contract’, in *International Encyclopaedia of Comparative Law*, vol. VII, *Contracts in General* (Tübingen, 1999), 15-16 to 15-19 and 15-124 to 15-128.

196 Law Commission, *Pecuniary Restitution on Breach of Contract* (Law Commission Report No. 121, London, 1983), 36-7.

197 *Cutter v. Powell* (1795) 6 Term Rep 320; 101 ER 573; M. Dockray, (2001) 117 LQR 664.

198 Mentioned by counsel in argument, citing Lord Holt in *Wiggins v. Ingleton* (1706) 2 Lord Raym 1211; 92 ER 300.

199 (1795) 6 Term Rep 320, 324.

But the Law Reform (Frustrated Contracts) Act 1943 now modifies the common law. The 1943 Act enables the court to award a 'just sum' in respect of the 'valuable benefit' conferred on the other party.²⁰⁰ Sometimes, the contract creates divisible obligations, that is, where 'different parts of the consideration may be assigned to severable parts of the performance, for example, an agreement for payment *pro rata*'.²⁰¹

17.53 The so-called 'substantial performance' doctrine might enable the performer to claim the agreed sum even if performance has not been perfect. Then the innocent party's protection is confined to a cross-claim or deduction in respect of defective performance.²⁰² But the doctrine of substantial performance will not apply if the failure to perform is significant:²⁰³ this depends on questions of proportionality, reasonableness and fairness.²⁰⁴ The doctrine is traceable to the eighteenth century.²⁰⁵ The three leading²⁰⁶ modern decisions are *Sumpter v. Hedges* (1898),²⁰⁷ *Bolton v. Mahadeva* (1972)²⁰⁸ and *Hoenig v. Isaacs* (1952)²⁰⁹ (despite the chronology, these cases will be examined in that sequence because substantial performance occurred only in the third of these cases).

17.54 In *Sumpter v. Hedges* (1898) a builder agreed to construct two houses for the defendant at a price of £565.²¹⁰ He performed £333 worth of this, but was forced to abandon the job because of lack of funds. The innocent party had already paid £219 (made up of £119 cash and two horses worth £100). The Court of Appeal held that the innocent party was not liable to pay the rest of the lump sum, because this obligation arose only on completion of the work. A claim for a *quantum meruit* (a restitutionary claim for the value of the services, and goods used) also failed because the builder's partial work (the partly finished building) had acceded to the defendant's land, and so the latter had not impliedly assumed a liability to pay a reasonable value for this partial performance (or become, to use the modern analysis, liable under restitutionary principles). But the defendant was liable to pay for loose materials left on site because he had freely decided to use these materials rather than returning them to a building merchant's yard and so 'cashing them in' and then crediting them to the builder or to his trustee in bankruptcy. In short, these

200 The leading case is *BP Exploration Co. (Libya) Ltd v. Hunt (No. 2)* [1979] 1 WLR 783, Goff J: the appellate decisions, [1981] 1 WLR 232, CA, and [1983] 2 AC 352, HL, do not affect Goff J's analysis of section 1(3) of the 1943 Act.

201 *Chitty on Contracts* (30th edn, London, 2008), 21-027.

202 *Hoenig v. Isaacs* [1952] 2 All ER 176, CA (discussed 17.56).

203 *Sumpter v. Hedges* [1898] 1 QB 673 (17.54).

204 As mentioned in *Bolton v. Mahadeva* [1972] 1 WLR 1010, CA (17.55).

205 *Boone v. Eyre* (1779) 1 Hy Bl 273n (summarised in the notes to *Cutter v. Powell* (1795) 6 Term Rep 320; *Smith's Leading Cases* (13th edn 1929); Lord Denning MR in '*The Hansa Nord*' [1976] 1 QB 44, 60, CA).

206 Other modern decisions: *Vigers v. Cook* [1919] 2 KB 475, 482, CA, *Williams v. Roffey & Nicholls (Contractors) Ltd* [1991] 1 QB 1, 17, CA, and *Pilbrow v. Pearless de Rougemont & Co.* [1993] 3 All ER 355, 361B, 360, CA.

207 [1898] 1 QB 673, CA.

208 [1972] 1 WLR 1010, CA.

209 [1952] 2 All ER 176, CA.

210 [1898] 1 QB 673, CA.

materials had not already acceded to his land (as where bricks and mortar now form a wall), but had been knowingly appropriated by the defendant.

- 17.55 In *Bolton v. Mahadeva* (1972), the claimant had agreed to fit a heating and domestic hot-water system for £560.²¹¹ After the job was 'done', the defendant refused to pay, because the heating system produced 10 per cent less warmth than required, and it also emitted fumes.²¹² The Court of Appeal held that the defendant's duty to pay the lump sum had not arisen on these facts. The level of defective performance was high. Cairns LJ, who gave the main reasoned judgment, said:²¹³ '[I]t is relevant to take into account both the nature of the defects and the proportion between the cost of rectifying them and the contract price. It would be wrong to say that the contractor is only entitled to payment if the defects are so trifling as to be covered by the *de minimis* rule.' Sachs LJ considered that the work had not merely been 'shoddy': it had failed to achieve 'its primary purpose' because the level of heating was inadequate and the appliance emitted fumes.²¹⁴ He also noted that the present litigation had arisen only because the contractor had stubbornly refused to remedy these defects.²¹⁵ Gareth Jones has suggested that 'proportionality' should not be the only criterion, and that the questions of unfair prejudice to the guilty party and the factor of adequacy of damages to the innocent party should also be considered.²¹⁶ These are all facets of the same inquiry: whether A's degree of inadequate or non-performance has deprived B of substantially the whole of the benefit for which B had stipulated and in return for which B's duty (normally to pay) is dependent.
- 17.56 On the other side of the line, in *Hoening v. Isaacs* (1952), the claimant agreed to redecorate and furnish the defendant's flat for £750.²¹⁷ The breach consisted of minor defects in the furniture provided by the claimant. But these could be rectified for £55. The Court of Appeal held that the claimant had a good claim for the price, subject to a deduction under a cross-claim of £55 in respect of the defective performance. In short, the job had been done in *Hoening* and the defects were relatively minor imperfections.

211 [1972] 1 WLR 1009, CA.

212 *Ibid.*, at 1013F.

213 *Ibid.*, at 1013E.

214 *Ibid.*, at 1015F.

215 *Ibid.*, at 1015H.

216 G. H. Jones (with P. Schlechtriem), 'Breach of Contract', in *International Encyclopaedia of Comparative Law*, vol. VII, *Contracts in General* (Tübingen, 1999), 15–19, noting Australian criticism.

217 [1952] 2 All ER 176, CA.

VIII

Remedies for breach

Chapter contents

1. Introduction *para.* 18.01
2. Debt claims *para.* 18.03
3. Specific Performance *para.* 18.13
4. Injunctions *para.* 18.20
5. Damages *para.* 18.23
6. Restitutionary claims *para.* 18.51
7. Declarations *para.* 18.62
8. 'Stays' upon legal proceedings *para.* 18.63
9. Interest on money claims *para.* 18.64

18

Judicial remedies for breach of contract

1. INTRODUCTION

18.01 This chapter concerns remedies awarded by the court (on application by an aggrieved party) for breach of contract. The next chapter will concern agreed remedies: payments of liquidated damages for breach, and forfeiture of deposits.

18.02 *The array of remedies for breach.* The five main¹ judicial remedies for breach of contract are as follows:

- (1) *The action for debt.* This is in practice the most common remedy of all. Michael Zander notes that county court debt actions increased² during the period 2004–7 to the 2 million level, having been approximately 1.8 million during the years 1999–2003. As for contract doctrine, the main controversy (18.05 ff) arising from debt claims concerns whether a party who has yet to complete performance can legitimately fulfil that task and earn the right to sue the other party for the agreed sum, even though the latter had earlier attempted to call off the job (an unaccepted repudiation, also known as an attempted anticipatory breach).
- (2) *Damages.* This is the common law claim for compensation; most textbooks devote most attention to this technically complex remedy. The main aim of compensatory damages is to place the promisee in the position he would have been in if the contract had been properly performed, the so-called ‘expectation’ or ‘loss of bargain’ measure (18.25). A subsidiary type of damages is to restore the claimant monetarily to the position he enjoyed before the contract was breached, the so-called ‘reliance loss’ measure (18.25, 18.26). Common to both of these measures of damages are the requirements that the loss should be:

¹ The minor remedies of declarations or ‘stays upon legal proceedings’ are noted at 18.62 and 18.63.

² M. Zander, ‘The Woolf Reforms: What’s the Verdict?’, in D. Dwyer (ed.), *Civil Procedure Rules Ten Years On* (Oxford, 2009), 417, at 427 n. 46 (his source for these figures being the annual *Judicial and Court Statistics*).

- (a) neither causally unrelated to the breach (18.39);
- (b) nor too remote (18.40);
- (c) nor based on a failure to mitigate loss (18.49).

Finally, if the claim could be based either on breach of contract or a failure in tort to exercise due care, damages can be reduced to reflect the claimant's contributory negligence (18.50).

- (3) *Specific performance*. This is an 'equitable remedy' (on the distinction between common law and equity, see 1.25). This is a draconian and potentially onerous remedy, requiring the defendant positively to act (18.19). Although this remedy upholds 'loyalty to promises', it has the disadvantage of enabling the claimant to insist on performance even though he could easily avoid, or at least reduce, his loss; and so specific performance relaxes the English system's general concern that the innocent party should take steps to mitigate his loss by entering the market for satisfaction from an alternative source (18.19). Specific performance is seldom encountered outside its heartland – contracts for the sale or exchange of interests in land (18.14). There can be no specific performance of contracts for personal services (18.17), nor against a company to require it to 'run a business' (18.19). Contracts to transfer movable property are remedied by damages awards, unless the subject matter is 'unique' or very nearly so (18.15).
- (4) *Injunction*. As just mentioned, specific performance is a mandatory injunction; other injunctions can be awarded to stop a party from breaching, or continuing to breach. If the claimant seeks it, an injunction to prevent a party breaching a promise not to do something is commonly granted, even though damages might have adequately protected the claimant's interests (18.21); but no such injunction will be granted if its indirect effect will be to coerce a person into performing a contract for personal services (18.22).
- (5) *An 'account of profits' based on the Blake principle*.³ In general, restitutionary claims operate independently of a breach of contract, for example to provide relief where a contract is invalid; only the restitutionary cause of action for an 'account of profits' (first applied in the *Blake* case (2001))⁴ (18.57 ff below) against the party in breach of contract has the element of breach as a constituent element. Although the equitable remedy of account can be used to 'disgorge' the gain made by the defendant in breach of contract, in fact this remedy is exceptional, indeed so much so that it is doubtful whether all the juristic fuss engendered by this decision has been 'worth it'; for, since the supposed remedial 'breakthrough' in the *Blake* case, the courts have tended not to award a complete disgorgement of gain based on the above-mentioned remedy of account. Instead, judges have found it preferable to award damages reckoned as the amount the defendant might reasonably have been expected to have paid the claimant for relaxation of the latter's rights (the so-called 'user principle' measure of damages: on which see 18.60 ff). Furthermore, the better

³ *Attorney-General v. Blake* [2001] 1 AC 268 HL.

⁴ *Ibid.*

view is that an award of ‘user principle’ damages is compensatory, that is, its aim is to indemnify the claimant for a real loss suffered (loss of a chance to exact a fee for a consensual release of rights); the claim is for loss suffered rather than gain obtained (irrespective of a corresponding loss).

SELECTED FURTHER READING

General

- N. Cohen and E. McKendrick (eds.), *Comparative Remedies for Breach of Contract* (Oxford, 2005)
- D. Saidov and R. Cunnington (eds.), *Contract Damages: Domestic and International Perspectives* (Oxford, 2008)
- A. S. Burrows, *Remedies for Torts and Breach of Contract* (3rd edn, Oxford, 2004)
- A. Burrows (ed.), *English Private Law* (2nd edn, Oxford, 2007), 21.17 to 21.71, 21.135 to 21.139 (on damages; now to be read in light of the *Transfield* case on remoteness and scope of duty); 18.43 case (5), 18.44 to 18.46, 21.167 to 21.174 (debt); 21.180 to 21.197 (specific performance); 21.200 to 21.206, 21.214 to 21.216 (injunctions); 21.156 to 21.159 (account of profits)
- D. Harris, D. Campbell and R. Halson, *Remedies in Contract and Tort* (2nd edn, London, 2002)
- C. Rickett (ed.), *Justifying Private Law Remedies* (Oxford, 2008)

Specific performance and injunctions

- A. S. Burrows, *Remedies for Torts and Breach of Contract* (3rd edn, Oxford, 2004), chapter 20
- A. Burrows (ed.), *English Private Law* (2nd edn, Oxford, 2007), 21.180 to 21.197 (specific performance); 21.200 to 21.206, 21.214 to 21.216 (injunctions)
- D. Friedmann, ‘Economic Aspects of Damages and Specific Performance Compared’, in D. Saidov and R. Cunnington (eds.), *Contract Damages: Domestic and International Perspectives* (Oxford, 2008), chapter 2
- D. Harris, D. Campbell and R. Halson, *Remedies in Contract and Tort* (2nd edn, London, 2002), chapter 12
- G. H. Jones and W. Goodhart, *Specific Performance* (2nd edn, London, 1996)

Expectation or performance interest damages for breach of contract

- D. Friedmann, ‘The Performance Interest in Contract Damages’ (1995) 111 LQR 628 (considering also the ‘classic’ article by Fuller and Perdue, ‘The Reliance Interest in Contract Damages’ (1936) 46 *Yale Law Journal* 52 and 373 (in two parts))

Date of assessment of damages

- M. Furmston, ‘Actual Damages, Notional Damages and Loss of a Chance’, in D. Saidov and R. Cunnington (eds.), *Contract Damages: Domestic and International Perspectives* (Oxford, 2008), 419, at 424 ff

- D. McLaughlan, 'Expectation Damages: Avoided Loss, Offsetting Gains and Subsequent Events', in D. Saidov and R. Cunnington (eds.), *Contract Damages: Domestic and International Perspectives* (Oxford, 2008), chapter 15
- C. J. Morgan, [2007] CLJ 263
- C. Nicholls, [2008] JBL 91
- B. Coote, (2007) 123 LQR 503
- M. Mustill, (2008) 124 LQR 569
- Sir Bernard Rix, 'Lord Bingham's Contributions to Commercial Law', in M. Andenas and D. Fairgrieve (eds.), *Tom Bingham and the Transformation of the Law: A Liber Amicorum* (Oxford, 2009), 679–83
- S. Waddams, 'The Date for the Assessment of Damages' (1981) 97 LQR 445

'Consumer surplus' damages

- D. Harris, A. Ogun and J. Phillips, 'Contract Remedies and the Consumer Surplus' (1979) 95 LQR 581, especially 580–6, 595–6, 604–10 (cited by Lord Millett in the *Panatown* case [2001] 1 AC 518, 589)

Disappointment damages in general

- D. Capper, (2002) 118 LQR 193–6
- E. McKendrick and M. Graham, 'The Sky's the Limit: Contractual Damages for Non-Pecuniary Loss' [2002] LMCLQ 161

Remoteness

- Lord Hoffmann, (2010) 14 *Edinburgh Law Review* 47–61
- D. Foxton, [2009] LMCLQ 461–87
- D. McLaughlan, (2009) 9 *Oxford University Commonwealth Law Journal* 109–39
- J. O'Sullivan, [2009] CLJ 34–7
- G. Gordon, (2009) *Edinburgh Law Review* 125–30
- E. Peel, (2009) 125 LQR 6–12
- A. Kramer, (2009) 125 LQR 408–15
- P. C. K. Wee, [2010] LMCLQ 150–76

Mitigation of loss

- M. Bridge, 'Mitigation of Damages in Contract and the Meaning of Avoidable Loss' (1989) 105 LQR 398
- M. Bridge, 'The Market Rule of Damages Assessment', in D. Saidov and R. Cunnington (eds.), *Contract Damages: Domestic and International Perspectives* (Oxford, 2008), chapter 18
- H. McGregor, 'The Role of Mitigation in the Assessment of Damages', in D. Saidov and R. Cunnington (eds.), *Contract Damages: Domestic and International Perspectives* (Oxford, 2008), chapter 14

Contributory negligence

C. Hopkins [1995] CLJ 20–3

A. S. Burrows, *Remedies for Torts and Breach of Contract* (3rd edn, Oxford, 2004), 136–44

Account of profits and gains-based claims

R. Goff and G. H. Jones, *The Law of Restitution* (7th edn, London, 2007), 20–024 to 20–034

A. Burrows, ‘Are “Damages on the Wrotham Park Basis” Compensatory, Restitutionary or Neither?’, in D. Saidov and R. Cunnington (eds.), *Contract Damages: Domestic and International Perspectives* (Oxford, 2008), chapter 7

S. Waddams, ‘Gains Derived from Breach of Contract: Historical and Conceptual Perspectives’, in D. Saidov and R. Cunnington (eds.), *Contract Damages: Domestic and International Perspectives* (Oxford, 2008), chapter 8

R. Cunnington, ‘The Measure and Availability of Gains-Based Damages for Breach of Contract’, in D. Saidov and R. Cunnington (eds.), *Contract Damages: Domestic and International Perspectives* (Oxford, 2008), chapter 9

J. Edelman, *Gain-Based Damages* (Oxford, 2002), chapter 5

Recovery of payment after failure of consideration

G. Virgo, in *Chitty on Contracts* (30th edn, London, 2008), 29–054 to 29–063; 29–074 to 29–075

A. Burrows, E. McKendrick and J. Edelman, *Cases and Materials on the Law of Restitution* (2nd edn, Oxford, 2007), 362–86

2. DEBT CLAIMS

18.03 Debt is the most important remedy because most claims for contractual default are attempts to obtain payment of specified sums (price, hire charges, insurance premium, rent, etc.). Debt claims are not classified as ‘equitable orders’ and so are not sanctioned ultimately by proceedings for contempt of court (18.13) if the defendant fails to comply. This contrasts with the position of the defendant who refuses to comply with specific performance and injunctions. Exceptionally, however, in *Beswick v. Beswick* (1968),⁵ a ‘money remedy’ was supported by an injunctive order, and hence ultimately sanctioned by contempt of court. In this case, the debtor had agreed to pay periodic sums to the promisee’s wife, a third party. The promisee’s estate successfully claimed that the debtor should be compelled, by order of specific performance, to continue paying periodical sums to this third party.

18.04 One of the rules within the so-called ‘penalty doctrine’ (19.03 ff, especially 19.16) is that a debtor cannot be required to pay a sum exceeding the principal and interest owed.

⁵ [1968] AC 58, HL.

- 18.05 A problematic aspect of contract law concerns the remedy for ‘debt’ and the principles of repudiatory breach. An innocent party has an ‘election’ – a choice – whether to ‘accept’ the repudiation or to ‘affirm’ the contract. This was the background to the majority House of Lords decision in *White & Carter v. McGregor* (1962).⁶

In *White & Carter v. McGregor* (1962), the ‘pursuer’ (a claimant in Scots legal terminology) sought payment of the price agreed for its advertising services. The ‘defender’ (a defendant in Scots legal terminology) had ordered these services but immediately tried to cancel the contract. The pursuer was not bound to ‘accept’, that is, acquiesce in, this proposed cancellation. Instead, the pursuer could legitimately complete performance and claim in debt for the agreed payment. An unusual feature of this situation was that the innocent party could complete his performance without any co-operation from the other party. In fact, the pursuer part-performed and the defender failed to pay the relevant instalment. An acceleration clause (19.18) rendered the defendant liable for all the instalments in the event of non-payment of one instalment. The majority (Lords Reid, Hodson and Tucker) upheld this acceleration clause, and further held that the pursuer was entitled to claim the full amount of the debt.

Three Law Lords (Lords Reid, Hodson and Tucker) held that an innocent party who elects not to terminate the contract, despite the other’s attempted repudiation, is entitled to complete a ‘solo’ performance (that is, without the other’s co-operation or involvement). He can then validly claim the agreed price for the completed job or task. The majority held that, in general, it does not matter that the other party had declared that he no longer wanted or needed the relevant performance. However, the two dissenting judges (Lords Morton and Keith) considered this claim for debt to be highly inefficient and unmeritorious. It would conflict with the economic goal of encouraging innocent parties to restrict their losses by ‘mitigating’ (generally on this doctrine, see 18.49). But the technical response to this dissenting argument is that the doctrine of mitigation is confined to claims for damages, and that the claimant is here asserting a right to a debt. Debt and damages are subject to different regimes.⁷

- 18.06 This last difference is clearly illustrated by *Reichman v. Beveridge* (2006).⁸ The Court of Appeal held that a landlord is entitled to sue for rent (an action in debt) for the residue

6 [1962] AC 413, HL; on which see *McGregor on Damages* (18th edn, London, 2009), 7-023 to 7-031; A. S. Burrows, *Remedies for Torts and Breach of Contract* (3rd edn, Oxford, 2004), 435–44 (citing US material at 437); Carter, Phang and Phang, (1999) 15 *Journal of Contract Law* 97; A. Tettenborn (ed.), *The Law of Damages* (London, 2003), 5.45 to 5.49; K. Scott, [1962] CLJ 12; P. M. Nienaber, [1962] CLJ 213; A. L. Goodhart, (1962) 78 LQR 263; M. Furmston, (1962) 25 MLR 364; Tabachnik, [1972] CLP 149; Priestley, (1991) 3 *Journal of Contract Law* 218; for references to US and Canadian materials or case law, see *Anson’s Law of Contract* (29th edn, Oxford, 2010), 575 n. 21 (US law, which differs from English law on this topic, was cited in *Clea Shipping Corporation v. Bulk Oil International* (*‘The Alaskan Trader’*) [1984] 1 All ER 129, 137, *per* Lloyd J).

7 On the differences between debt and damages, see Millett LJ in *Jervis v. Harris* [1996] Ch 195, 202–3, CA.

8 [2006] EWCA Civ 1659; [2007] 1 P & CR 20; [2007] L & TR 18 (critically noted by M. Pawlowski, (2010) 126 MLR 361–5 on the proposition that a landlord cannot recover damages for loss of future rent).

of a business tenancy. The landlord is under no obligation to mitigate by accepting the tenant's attempted renunciation. The landlord does not act unreasonably by insisting on its right to keep open the tenancy and to maintain its right to rent. On this last point, the decision is another application, on this occasion in favour of the innocent party, of the 'legitimate interest' test, introduced by Lord Reid in the *White & Carter* case (1962). This test is examined at 18.09 to 18.12 below.

- 18.07** Since the *White & Carter* case (1962) (introduced at 18.05), the cases have established that there are two restrictions upon the innocent party's opportunity to take advantage of this rule:⁹ (1) the claimant cannot succeed in suing for debt if his performance requires the other party's co-operation; and (2) the claimant must show a 'legitimate interest' in pursuing his unwanted performance. The second requirement will be applied quite generously in favour of the innocent party (but this approach is criticised at 18.11).
- 18.08** *Case law development of the 'co-operation' qualification.* In *Hounslow London Borough Council v. Twickenham Garden Developments Ltd* (1971), Megarry J held that a builder could not perform once the owner of the site had ordered him to stop work.¹⁰ In *Ministry of Sound (Ireland) v. World Online Ltd* (2003),¹¹ Nicholas Strauss QC, sitting as a Deputy High Court Judge, held that a packaging company had a *prima facie* valid claim – the decision was an appeal from a pre-trial order – for the last instalment under a two-year contract requiring it to package and distribute, and give publicity to, the defendant's CDs. The defendant could not factually obstruct the substance of the claimant's performance (continuing to give publicity to the defendant's product). The claimant now found it unnecessary to do the primary task (distributing CDs, which the defendant had now ceased to supply). This was a situation where the claimant was able to continue performance of its side of the bargain despite the defendant's attempted repudiation. The judge also held that the claimant had a legitimate interest in so doing¹² (see further 18.09).
- 18.09** *Innocent party lacking a 'legitimate interest'.* As the Court of Appeal in *Reichman v. Beveridge* (2006) noted,¹³ explaining the genesis of this second requirement, only Lord Reid in *White & Carter v. McGregor* (1962)¹⁴ had ventured this idea, 'neither Lord Hodson nor Lord Tucker [the other members of the majority] alluded to such a possibility'. For this reason, the Supreme Court could yet decide that the law should be wholly remoulded (see 18.12). In the *White & Carter* case (1962), Lord Reid said:

⁹ A. S. Burrows, *Remedies for Torts and Breach of Contract* (3rd edn, Oxford, 2004), 433–40.

¹⁰ [1971] Ch 233, 253–4.

¹¹ [2003] EWHC 2178; [2003] 2 All ER (Comm) 823.

¹² *Ibid.*, at [64] to [66].

¹³ [2006] EWCA Civ 1659; [2007] 1 P & CR 20; [2007] L & TR 18, at [14].

¹⁴ [1962] AC 413, 431, HL.

It may well be that, if it can be shown that a person has no legitimate interest, financial or otherwise, in performing the contract rather than claiming damages, he ought not to be allowed to saddle the other party with an additional burden with no benefit to himself. If a party has no interest to enforce a stipulation, he cannot in general enforce it: so it might be said that, if a party has no interest to insist on a particular remedy, he ought not to be allowed to insist on it. And just as a party is not allowed to enforce a penalty, so he ought not to be allowed to penalise the other party by taking one course when another is equally advantageous to him.

Simon J in *'The Dynamic'* (2003) formulated the following principle:¹⁵

- (1) The burden is on the contract-breaker to show that the innocent party has no legitimate interest in performing the contract rather than claiming damages.
- (2) This burden is not discharged merely by showing that the benefit to the [innocent party] is small in comparison to the loss to the contract breaker.
- (3) The exception to the general rule applies only in extreme cases: where damages would be an adequate remedy and where an election to keep the contract alive would be unreasonable.

And the Court of Appeal in *Reichman v. Beveridge* (2006) said:¹⁶

There is, therefore, a very limited category of cases [where] ... an election to keep the contract alive would be wholly unreasonable and ... damages would be an adequate remedy, or that the [innocent party] would have no legitimate interest in making such an election.

- 18.10 Cases concerning this restriction are conveniently summarised in *Reichman v. Beveridge* (2006).¹⁷ Two reported decisions (see cases (1) and (2) set out below) have fettered the performing party's power to keep open the contract and sue for a debt (although the tenor of the case law is that this should be an 'exceptional' fetter) (see cases (3), (4) and (5) set out below). It will be contended below that the law should be altered in favour of maintaining this fetter upon requiring a party to pay for unwanted performance.

The 'no legitimate interest' cases

- (1) There are *dicta* applying this restriction against the innocent party in *Attica Sea Carriers Corporation v. Ferrostaal Poseidon Bulk Reederei GmbH ('The Puerto Buitrago')* (1976).¹⁸

15 *Ocean Marine Navigation Ltd v. Koch Carbon Inc. ('The Dynamic')* [2003] EWHC 1936; [2003] 2 Lloyd's Rep 693, at [23], *per* Simon J.

16 [2006] EWCA Civ 1659; [2007] 1 P & CR 20; [2007] L & TR 18, at [17].

17 *Ibid.*, at [16].

18 [1976] 1 Lloyd's Rep 250, CA.

This case concerned a demise charterparty. The contract provided that the ship should be repaired at the end of the hire period at the charterer's expense. The charterer attempted to return the ship without repairs. The cost of repair (US\$2 million) would exceed the ship's value (US\$1 million). The Court of Appeal held that the owner's right to demand repair work had not in fact arisen. The court added *dicta* suggesting that the owner's insistence on repairing the ship at the charterer's expense would have been objectionable because it would involve an indirect form of specific performance of the charterer's obligation to repair and, on the facts, the owner lacked any legitimate interest in keeping the vessel on hire.¹⁹

(2) The legitimate interest criterion was also held to fetter the owner on the facts of *Clea Shipping Corporation v. Bulk Oil International* ('*The Alaskan Trader*') (1984):²⁰

This case concerned a two-year time charterparty. In the second year, the vessel suffered serious engine failure. It was taken off-hire for repair. The charterers attempted to renounce the contract. But the owner redelivered the vessel, with a full crew, to the charterers for the remaining months of the contract. Lloyd J suggested that the 'legitimate interest' restriction would apply only in 'extreme cases, viz. where damages would be an adequate remedy and where an election to keep the contract alive' would be 'wholly unreasonable', 'quite unrealistic' and 'untenable'. Lloyd J decided not to disturb the arbitrator's view that the owner lacked a legitimate interest in continuing to charge hire on these facts: 'the arbitrator has found, and found clearly, that the owners had no legitimate interest in pursuing their claim for hire. In my view that finding is conclusive of this appeal ... It was the arbitrator who heard the evidence over many days; not me. It was for him to decide.'

It appears that decisions (1) and (2) above should be regarded as exceptional, in light of cases (3), (4) and (5) below. As for case (1), it would have been economically wasteful to have kept the contract alive and insisted on £2m of repair work by the charterer, resulting in a ship worth only £1m. As for case (2), Lloyd J's decision is tentative: he merely acquiesced in the arbitrator's decision, making clear that he had no strong views himself. It would be wrong to deduce from these exceptional cases that Lord Reid's 'legitimate interest' idea (18.09) will be used extensively in favour of a party who has attempted to repudiate. Clearer guidance is provided by the next three decisions.

'Performer enjoying a legitimate interest'

(3) In '*The Odenfeld*' (1978),²¹ Kerr J held that the performer did have a legitimate interest to press on with performance on these facts. This case concerned a time charterparty

¹⁹ *Ibid.*, at 255.

²⁰ [1984] 1 All ER 129, 136–7, Lloyd J.

²¹ *Gator Shipping Corporation v. Trans-Asiatic Oil Ltd SA and Occidental Shipping Establishment* ('*The Odenfeld*') [1978] 2 Lloyd's Rep 357, 373, Kerr J.

which began in 1973. In 1975, the freight market collapsed. In 1976, the charterers repudiated. Kerr J regarded the 'no legitimate interest' fetter as applicable only in 'extreme cases, viz. where damages would be an adequate remedy and where an election to keep the contract alive would be wholly unreasonable'.²² He upheld the arbitrator's decision that the owner did have a 'legitimate interest' in maintaining the vessel on hire to the charterer until September 1976.

(4) Simon J's decision in *'The Dynamic'* (2003) reaffirms the innocent party's general right to sue for hire, despite a charterer's attempt to end the contract.²³ Simon J remitted a dispute to the arbitrator for reconsideration. The question in this case was whether the owner was required to accept a charterer's attempted premature redelivery of the ship, in breach of contract, or whether the owner could legitimately regard the vessel as still on hire. The dispute was complicated by the fact that the vessel had been arrested at the time of the purported redelivery. The arbitrator had found in favour of the charterers, deciding that an owner could not legitimately, on the relevant facts, elect to maintain the contract and keep a vessel on hire. But, on appeal, Simon J said that there was no indication that the arbitrator had correctly applied the 'legitimate interest' test (as Simon J formulated it: see the quotation at 18.09 above).

(5) On this rather ragged line of cases, the Court of Appeal in *Reichman v. Beveridge* (2006) said (see further 18.12 on that case):²⁴ 'There is, therefore, a very limited category of cases [where] ... an election to keep the contract alive would be wholly unreasonable and ... damages would be an adequate remedy, or that the [innocent party] would have no legitimate interest in making such an election'.

- 18.11 *Assessment of the 'legitimate interest' criterion.* Putting aside the two exceptional decisions in *Attica Sea Carriers* (1976) and *'The Alaskan Trader'* (1984) (cases (1) and (2) above), the other decisions show a reluctance to protect parties in breach in this context (the innocent party being entitled to performance unless this would be 'wholly unreasonable': see the quotations at cases (3), (4) and (5) above). However, is the law on this point attractive? Might it be changed? In *Ministry of Sound (Ireland) v. World Online Ltd* (2003),²⁵ Nicholas Strauss QC, said: 'The commercially just result would be to restrict the innocent party to its claim for damages. But I am far from convinced that, as a general rule, English contract law in this area is designed always to achieve the commercially just result.' This is a persuasive hint by a leading commercial lawyer that the correctness of the *White & Carter* decision (1962) should be reconsidered by the Supreme Court (interestingly, the Scottish Law Commission has recommended reform).²⁶

²² *Ibid.*, at 374.

²³ *Ocean Marine Navigation Ltd v. Koch Carbon Inc. ('The Dynamic')* [2003] EWHC 1936; [2003] 2 Lloyd's Rep 693, at [23], per Simon J.

²⁴ [2006] EWCA Civ 1659; [2007] 1 P & CR 20; [2007] L & TR 18, at [17].

²⁵ *Ibid.*, at [61].

²⁶ L. McGregor, in J. Smits, D. Haas and G. Heslen (eds.), *Specific Performance in Contract Law: National and Other Perspectives* (Antwerp, 2008), 67, 89, noting *Report on Remedies for Breach of Contract* (Scottish Law Commission Report No. 174, Edinburgh, 1999), Part II.

It is submitted that the innocent party should only be allowed to maintain the contract if he can show that damages, assessed at the date of the attempted renunciation, would not properly protect an important commercial or other significant interest (mere difficulty in assessing damages should not be sufficient: damages can be awarded despite difficulty in assessment). The innocent party's important commercial or other significant interest should have been known to the guilty party, or be reasonably obvious to him. Instead, the innocent party should normally obtain compensation, rather than be permitted stubbornly to 'hold out' for eventual complete payment of the agreed remuneration. Indeed, other systems have refused to follow the lead of English (and Scots) law in making this distinction in the reach of mitigation between debt and damages claims.²⁷ And so a management consultant should not be free to go to Hong Kong and make a report into a third party company if the commissioning party has decided to call off the engagement, the example given by Lord Reid in the *White & Carter* case (1962):

Then it was said that, even where the innocent party can complete the contract without such co-operation, it is against the public interest that he should be allowed to do so. An example was developed in argument. A company might engage an expert to go abroad and prepare an elaborate report and then repudiate the contract before anything was done. To allow such an expert then to waste thousands of pounds in preparing the report cannot be right if a much smaller sum of damages would give him full compensation for his loss. It would merely enable the expert to extort a settlement giving him far more than reasonable compensation.²⁸

Nor should a surveyor be free to make a report on a property which the client is no longer interested in buying.

- 18.12 The innocent party's interest in upholding the contract will be legitimate if damages are inadequate or unavailable. On this basis, the decision in the *Reichman* case (2006)²⁹ is correct: a landlord should not be required to find a new business tenant, because landlords have no right to compensation in respect of future loss of rent, as Lloyd LJ noted in the *Reichman* case (2006),³⁰ although this last proposition has been contested by one commentator.³¹ Indeed, the landlord will require guarantees from third parties to secure the tenant's continuing payment of rent. In this way, business leases are structured to ensure a flow of rent, should the tenant default.

27 *Anson's Law of Contract* (29th edn, Oxford, 2010), 575 n. 21, citing US and Canadian materials or case law.

28 [1962] AC 413, 428–9, 442, HL, *per* Lord Reid (Lord Keith also quoting this example).

29 [2006] EWCA Civ 1659; [2007] 1 P & CR 20; [2007] L & TR 18.

30 *Ibid.*, at [18].

31 M. Pawlowski, (2010) 126 MLR 361–5, citing various authorities inconsistent with the proposition that a landlord cannot recover damages for loss of future rent.

18.13 *Specific performance: contempt of court doctrine for breach of injunctions or orders for specific performance.*³² A person will be guilty of contempt of court (and become a 'contemnor') if he breaches an injunction (18.20) or an order of specific performance³³ addressed to him. A 'contemnor' can be committed for contempt of court,³⁴ a quasi-criminal wrong for which the standard of proof is 'beyond reasonable doubt' rather than the lower civil standard of proof 'on the balance of probabilities'.³⁵ The court can apply the following sanctions: the contemnor can be imprisoned for up to two years;³⁶ or fined; or, in the case of both individuals³⁷ and companies, the court can order 'sequestration' of their assets³⁸ ('sequestrators', officers of the court, often appointed specially for the present case, can then seize the contemnor's property, including land,³⁹ and eventually sell it).⁴⁰ When deciding on the appropriateness of punishing the contemnor, the following will be relevant: (1) the contemnor has 'contumeliously' flouted the law;⁴¹ (2) it has become evident that he will not accept the court's authority; (3) the contemnor has already received adequate punishment;⁴² (4) he has 'purged' his contempt;⁴³ and (5) his conduct or omission was deliberate or negligent.⁴⁴ As for this last consideration, inadvertent breach of an injunction will not normally justify punishment.⁴⁵

18.14 *Main criteria for specific performance.* This remedy is available only if the contract is supported by consideration and the remedies of damages or debt would provide inadequate

32 Arlidge, *Eady and Smith on Contempt* (3rd edn, London, 2005).

33 G. H. Jones and W. Goodhart, *Specific Performance* (2nd edn, London, 1996); A. S. Burrows, *Remedies for Torts and Breach of Contract* (3rd edn, Oxford, 2004), chapter 20; D. Harris, D. Campbell and R. Halson, *Remedies in Contract and Tort* (2nd edn, London, 2002), chapter 12; D. Friedmann, 'Economic Aspects of Damages and Specific Performance Compared', in D. Saidov and R. Cunningham (eds.), *Contract Damages: Domestic and International Perspectives* (Oxford, 2008), chapter 2; comparative account: J. Smits, D. Haas and G. Heslen (eds.), *Specific Performance in Contract Law: National and Other Perspectives* (Antwerp, 2008); G. H. Treitel, *Remedies for Breach of Contract: A Comparative Account* (Oxford, 1988) (see also *ibid.*, at 63 ff for a comparative discussion concerning the common law); E. Yorio, *Contract Enforcement: Specific Performance and Injunctions* (New York, 1989); on the nineteenth-century history of this topic, see M. Lobban, in W. Cornish, J. S. Anderson, R. Cocks, M. Lobban, P. Polden and K. Smith, *The Oxford History of the Laws of England*, vol. XII, 1820–1914: *Private Law* (Oxford, 2010), 548 ff.

34 RSC Order 52 in Schedule 1 to the CPR; and CCR Order 29 in Schedule 2 to the CPR.

35 *Z Bank v. DI* [1974] 1 Lloyd's Rep 656, 660, Colman J.

36 *Harris v. Harris* [2001] EWCA Civ 1645; [2002] Fam 253, CA, at [12] to [14], noting section 14(1) of the Contempt of Court Act 1981, restricting the period to a maximum of two years' imprisonment.

37 *Raja v. Van Hoogstraten* [2004] EWCA Civ 968; [2004] 4 All ER 793, at [71] ff.

38 RSC Order 45, rules 3(1)(c), 4(2)(c) and 5(1)(b)(i)(ii); RSC Order 46, rule 5; on the court's inherent power, see *Webster v. Southwark London Borough Council* [1983] QB 698.

39 *Mir v. Mir* [1992] Fam 79.

40 On sequestrators' potential liability for negligence, see *IRC v. Hoogstraten* [1985] QB 1077, CA; *Raja v. Van Hoogstraten* [2007] EWHC 1743 (Ch).

41 *Bhimji v. Chatwani* [1991] 1 WLR 989; *Watkins v. AJ Wright (Electrical) Ltd* [1996] 3 All ER 31; on the question when a litigant's defiance in open court of a judicial or court order will justify imprisonment for contempt, see *Bell v. Tuohy* [2002] EWCA Civ 423; [2002] 3 All ER 975, CA, at [60] to [66].

42 *Re Barrell Enterprises* [1973] 1 WLR 19, CA; RSC Order 52, rule 8.

43 *Harris v. Harris* [2001] EWCA Civ 1645; [2002] Fam 253, CA (the court lacks the power to permit the release of a contemnor from prison on condition that he does not commit a fresh contempt).

44 *Guildford Borough Council v. Valler*, *The Times*, 15 October 1993, CA.

45 *E.g. Adam Phones Ltd v. Gideon Goldschmidt* (unreported, 9 July 1999) (innocent failure to comply with a court order for delivery up of materials).

relief. Specific performance is the primary remedy only in the context of agreements for the transfer of land or shares in *private* companies.⁴⁶ In those situations, the relevant subject matter is, or is regarded as, 'unique'.

18.15 *Scarce goods*.⁴⁷ Specific performance is not awarded to compel transfers of chattels unless they are special, indeed 'unique' (for example, 'Princess Diana's wedding dress' or Bobby Moore's World Cup winner's medal).⁴⁸ Reported cases have produced an eclectic collection: unusual china jars;⁴⁹ stones from old Westminster Bridge;⁵⁰ an Adam-style door;⁵¹ and a 'practically unique' ship.⁵² But, in general, the duty to mitigate (18.49) requires the disappointed buyer of a chattel, or of a commodity, to enter the market and find a substitute supplier. Unless the subject matter is 'unique', the disappointment buyer is confined to his remedy in damages, and this is so even if he can show a convincing 'sentimental attachment' to the relevant chattel. However, Burrows finds this too rigid.⁵³

18.16 The general refusal to order specific performance of agreements for the transfer of movable property is reasonable. This is because the subject matter is generic or fungible, and hence easily substituted. However, sometimes even fungibles can become alarmingly scarce. This can justify exceptional relief. Thus, in *Sky Petroleum Ltd v. VIP Petroleum Ltd* (1974), Goulding J recognised that exceptional market conditions can render damages an inadequate remedy for default even in the supply of a commodity.⁵⁴ As a result of steps taken by the OPEC cartel during the 1970s 'oil crisis', wholesale petrol supplies had become scarce. Unless it gained the present remedy, the claimant would have been forced out of business.⁵⁵ Goulding J awarded an interim injunction, equivalent to specific performance, to compel an oil supplier to deliver petrol to a retailer.⁵⁶ But even that extreme case is open to doubt, in light of the later Court of Appeal decision in *Société des Industries Metallurgiques SA v. Bronx Engineering Co.*

46 For specific performance to compel the transfer of shares in a *private* company, see *Harvela v. Royal Trust Bank of Canada* [1986] AC 207, HL.

47 G. H. Jones and W. Goodhart, *Specific Performance* (2nd edn, London, 1996), 143–54.

48 The history of English performances since 1966 underlines the continuing 'uniqueness' of that medal.

49 *Falcke v. Gray* (1859) 4 Drew 651.

50 *Thorn v. Public Works Commissioners* (1863) 32 Beav 490.

51 *Phillips v. Lamdin* [1949] 2 KB 33, 41, Croom-Johnson J.

52 *Behnke v. Bede Shipping Co. Ltd* [1927] 1 KB 649, Wright J; this test was not satisfied in '*The Stena Nautica*' (No. 2) [1982] 2 Lloyd's Rep 336, Parker J; cf the wide *dictum* of Browne-Wilkinson V-C in *Bristol Airport plc v. Powdrill* [1990] Ch 744, 759 CA (lease of an aircraft is specifically enforceable; every aircraft is unique; but ship cases not cited).

53 A. S. Burrows, *Remedies for Torts and Breach of Contract* (3rd edn, Oxford, 2004), 464, suggesting that the 'consumer surplus' factor might be borne in mind here: on which see 18.34.

54 [1974] 1 WLR 576, Goulding J, where the goods were not even 'specific or ascertained' for the purpose of section 52 of the Sale of Goods Act 1979; *Re Wait* [1927] 1 Ch 606, CA (specific performance unavailable outside the limits of that provision); generally, see Treitel, [1966] JBL 211, A. S. Burrows, *Remedies for Torts and Breach of Contract* (3rd edn, Oxford, 2004), 462 ff, and R. Halson, *Contract Law* (London, 2001), 445–7.

55 [1974] 1 WLR 576, 578–9, Goulding J.

56 *Ibid.*

Ltd (1975).⁵⁷ The court held that damages would be adequate when a seller refused to supply machinery, even though it would take almost a year for an alternative manufacturer to supply the claimant. Burrows commented on this decision: '[T]he plain truth seems to be that the Court of Appeal was here rejecting "commercial" as opposed to "physical" uniqueness.'⁵⁸ However, Burrows attractively contends that 'commercial uniqueness' should be a ground for the award of specific performance if 'an accurate assessment of the claimant's losses is so difficult that [he] is likely to be incorrectly compensated'.⁵⁹

- 18.17 Even if the relevant type of contract is one where specific performance is available in principle, the court will be guided by various subsidiary factors when deciding whether to exercise its 'discretion' to order specific performance:⁶⁰ whether the claimant's conduct has been unmeritorious ('lack of clean hands'); delay; acquiescence; 'mutuality' (that is, when the claimant, who is seeking specific performance, has yet to fulfil his side of the bargain, and the court must consider whether the defendant is protected against the risk of default by the claimant);⁶¹ vagueness; problems of continuing supervision; and hardship (see 16.31 on *Patel v. Ali* (1984)).⁶² On these grounds for denial of the remedy, Lord Hoffmann commented in *Co-operative Insurance Services v. Argyll Stores Ltd* (1998): 'Of course the grant or refusal of specific performance remains a matter for the judge's discretion. There are no binding rules, but this does not mean that there cannot be settled principles, founded upon practical considerations of the kind which I have discussed, which do not have to be re-examined in every case, but which the courts will apply in all but exceptional circumstances.'⁶³ Claims for injunctive relief or specific performance are subject to the equitable bars of laches and acquiescence, and the statutory periods of limitation do not apply.⁶⁴ Specific performance is certainly unavailable to compel an individual to perform personal services, for example to work for an employer (and see the discussion of injunctions below).⁶⁵ In the case of contracts of employment, this restriction is enshrined in the Trade Union and Labour Relations (Consolidation) Act 1992, section 236 of which states:

⁵⁷ [1975] 1 Lloyd's Rep 465, CA.

⁵⁸ A. S. Burrows, *Remedies for Torts and Breach of Contract* (3rd edn, Oxford, 2004), 463.

⁵⁹ *Ibid.*

⁶⁰ *Co-operative Insurance Society v. Argyll Stores (Holdings) Ltd* [1998] AC 1, HL, noted by G. H. Jones, [1997] CLJ 488; *Rainbow Estates Ltd v. Tokenhold Ltd* [1999] Ch 64, 68G–74; *Beswick v. Beswick* [1968] AC 58, HL; *Price v. Strange* [1978] Ch 337, CA; *Tito v. Waddell (No. 2)* [1977] Ch 106, 321–8, Megarry V-C; *Verrall v. Great Yarmouth District Council* [1980] 1 All ER 839, CA; *Posner v. Scott-Lewis* [1987] Ch 25, Mervyn-Davies J, noted by G. H. Jones, [1987] CLJ 21–3.

⁶¹ *Price v. Strange* [1978] Ch 337, CA.

⁶² [1984] Ch 283, Goulding J.

⁶³ [1998] AC 1, 16, HL.

⁶⁴ *P&O Nedlloyd BV v. Arab Metals Co.* [2006] EWCA Civ 1717; [2007] 1 WLR 2288; for a short statement of the limitation rules, see N. Andrews, *The Modern Civil Process* (Tübingen, 2008), 3.09 ff; for literature and other authorities, see N. Andrews, *English Civil Procedure* (Oxford, 2003), 12.81 ff; Law Commission, *Limitation of Actions* (Law Commission Report No. 270, London, 2001), 2.97 to 2.99.

⁶⁵ G. H. Jones and W. Goodhart, *Specific Performance* (2nd edn, London, 1996), 169–83; P. Saprui, 'The Principle against Self-Enslavement in Contract Law' (2009) 26 *Journal of Contract Law* 25–44.

No court shall, whether by way of—

- (a) an order for specific performance ... of a contract of employment, or
- (b) an injunction ... restraining a breach or threatened breach of such a contract,

compel an employee to do any work or attend at any place for the doing of any work.

18.18 Some commentators wrongly thought that the House of Lords decision in *Beswick v. Beswick* (1968) might have heralded a major expansion of specific performance (on this case, see 7.22).⁶⁶ For example, F. H. Lawson suggested in 1972 and in 1980:⁶⁷ '[I]t is not unreasonable to see in [this decision] an acknowledgement of a right to specific performance of all contracts where there is no adequate reason for the courts to refuse it.' In fact, no such major extension of this remedy occurred. Instead, the House of Lords in *Co-operative Insurance Services v. Argyll Stores Ltd* (1998) (see the next paragraph), the leading modern decision, rejected a major expansion of this remedy's scope.⁶⁸ As for clauses stipulating that specific performance should be available, Solène Rowan has challenged the view that the courts will not countenance a usurpation of their discretionary control of the award of specific performance, and has shown that in some commercial contexts American law has upheld such a stipulation.⁶⁹ These are the leading judicial comments on this topic.

In *Quadrant Visual Communications Ltd v. Hutchison Telephone (UK) Ltd* (1993), Stocker LJ said:⁷⁰

Once the court is asked for the equitable remedy of specific performance, its discretion cannot be fettered. Once the assistance of the court is invoked by one of the parties in a discretionary matter, that party is bound by the general discretion of the court to grant or refuse the remedy sought. If ... [the] submission that the court is bound by the terms of the contract and therefore has no discretion to exercise is correct, the function of the court would be reduced to that of a rubber stamp. In my opinion, this could not be and is not the situation.

In *Warner Bros Pictures Inc. v. Nelson* (1937), Branson J said:⁷¹

Of course, parties cannot contract themselves out of the law; but it assists, at all events, on the question of evidence as to the applicability of an injunction in the present case, to find the parties formally recognizing that in cases of this kind injunction is a more appropriate remedy than damages.

⁶⁶ *Beswick v. Beswick* [1968] AC 58, HL.

⁶⁷ F. H. Lawson, *Remedies of English Law* (2nd edn, London, 1980), 223.

⁶⁸ *Co-operative Insurance Society v. Argyll Stores (Holdings) Ltd* [1998] AC 1, HL, noted by G. H. Jones, [1997] CLJ 488.

⁶⁹ S. Rowan, 'For the Recognition of Remedial Terms Agreed Inter Partes' (2010) 126 LQR 448, 449–55, 470–5.

⁷⁰ [1993] BCLC 442, 451, CA.

⁷¹ [1937] 1 KB 209, 220–1.

- 18.19 *Co-operative Insurance Services v. Argyll Stores Ltd (1998)*. In this important case, the House of Lords held that specific performance is not available to compel a tenant to honour a long-running covenant to 'keep open' a business.

The *Co-operative Insurance* case concerned a lease for a supermarket site in a Sheffield shopping mall. The thirty-five-year lease, granted in 1979, included a clause that the tenant would continue trading for the same period (a so-called 'keep open' clause). The relevant clause stated: '[The tenant will] keep the demised premises open for retail trade during the usual hours of business in the locality [and it will keep] the display windows properly dressed in a suitable manner in keeping with a good class parade of shops.' Another clause required the tenant to offer a 'full range of grocery provisions'.

In 1994, when the tenancy still had more than nineteen years to run, the defendant supermarket chain handed back the keys to the landlord. The claimant landlord sought specific performance (generally on this remedy, see 18.13) to force the defendant to trade at this site until 2014, or until it sublet or assigned to another supermarket company. The House of Lords held that specific performance could not be granted in this context and, furthermore, the relevant clause was insufficiently precise.

The House of Lords decision reversed the Court of Appeal's majority decision to order specific performance in view of the defendant's 'gross commercial cynicism' and the fact that they had behaved 'very badly'.⁷² The Court of Appeal's decision had come as a great surprise. This was because it had been 'the settled and invariable practice of the court never to grant mandatory injunctions requiring those persons to carry on business', and instead the innocent party was confined to a remedy in damages.⁷³ The House of Lords decision, therefore, restored this 'settled and invariable practice'.

The House of Lords noted that specific performance is unavailable to compel someone to continue to run a business. And so damages alone were available. Lord Hoffmann (with whom the other Law Lords simply concurred) gave as one of his reasons for withholding specific performance the fact that this remedy requires the contractual terms to be very clear (for discussion of this case in respect of 'certainty', see 4.25). Otherwise, the courts will become embroiled in a litany of minor complaints and counter-arguments. Lord Hoffmann regarded this keep open clause as insufficiently precise: '[T]his language seems to me to provide ample opportunity for argument over whether the defendant is doing enough to comply with the order.'⁷⁴

⁷² [1996] Ch 286, 295, CA, *per* Leggatt and Roch LJ, respectively.

⁷³ On that 'invariable practice', see Millett LJ, the dissenter, at [1996] Ch 286, 302.

⁷⁴ [1998] AC 1, 17, HL; such 'keep open' clauses are specifically enforced in Scotland: *Highland & Universal Properties Ltd v. Safeway Properties Ltd*, 2000 SLT 414; *Co-operative Insurance Society Ltd v. Halfords Ltd (No. 2)*, 1999 SLT 685, OH; *Estates Gazette*, 12 July 2003.

Lord Hoffmann's speech in *Co-operative Insurance Services v. Argyll Stores Ltd* (1998) contains many lucid and compelling observations on the appropriate scope of specific performance, not just in the immediate context of that case, but more generally. The following passages are especially important.

On the residual status of the equitable remedy of specific performance, Lord Hoffmann said:

Specific performance is traditionally regarded in English law as an exceptional remedy, as opposed to the common law damages to which a successful plaintiff is entitled as of right ...

By the 19th century it was orthodox doctrine that the power to decree specific performance was part of the discretionary jurisdiction of the Court of Chancery to do justice in cases in which the remedies available at common law were inadequate. This is the basis of the general principle that specific performance will not be ordered when damages are an adequate remedy.⁷⁵

On the punishment of defendants not being the aim of private law remedies, Lord Hoffmann said:

It is true that the defendant has, by his own breach of contract, put himself in such an unfortunate position. But the purpose of the law of contract is not to punish wrongdoing but to satisfy the expectations of the party entitled to performance. A remedy which enables him to secure, in money terms, more than the performance due to him is unjust.

On the problem of the need for the constant supervision of an order to continue an activity, as distinct from an obligation to achieve a measurable result, Lord Hoffmann said:

The most frequent reason given in the cases for declining to order someone to carry on a business is that it would require constant supervision by the court ... Supervision would in practice take the form of rulings by the court ... as to whether there had been a breach of the order. It is the possibility of the court having to give an indefinite series of such rulings in order to ensure the execution of the order which has been regarded as undesirable.⁷⁶

And:

The possibility of repeated applications over a period of time means that, in comparison with a once-and-for-all inquiry as to damages, the enforcement of the remedy is likely to be expensive in terms of cost to the parties and the resources of the judicial system ...⁷⁷

⁷⁵ [1998] AC 1, 11.

⁷⁶ *Ibid.*, at 12.

⁷⁷ *Ibid.*, at 40.

[One must] distinguish between orders which require a defendant to carry on an activity, such as running a business over a more or less extended period of time, and orders which require him to achieve a result ...⁷⁸

This distinction between orders to carry on activities and orders to achieve results explains why the courts have in appropriate circumstances ordered specific performance of building contracts and repairing covenants.⁷⁹

However, Burrows is deeply sceptical of this suggested distinction.⁸⁰ Certainly, the distinction between ‘activities’ and ‘achieving a result’ is a matter of degree: polishing a table or perhaps thatching a roof, and even a promise to build a ‘five-bedroom house to the highest modern standards’ would exemplify ‘achieving a result’; but not running a business for a period of years; and what would be the position concerning an undertaking to ‘design and construct a modern kitchen table, the product to be available for wholesale production’?

On the disproportion between harm to the defendant and loss to the claimant, Lord Hoffmann said:

The loss which the defendant may suffer through having to comply with the order (for example, by running a business at a loss for an indefinite period) may be far greater than the plaintiff would suffer from the contract being broken.⁸¹

On the danger of exposing the defendant to oppression, Lord Hoffmann said:

[The court should not] deliver over the defendants to the plaintiff bound hand and foot, in order to be made subject to any extortionate demand that he may possibly make.⁸²

And on the draconian sanction of contempt of court, Lord Hoffmann said:

The only means available to the court to enforce its order is the quasi-criminal procedure of punishment for contempt. This is a powerful weapon; so powerful, in fact, as often to be unsuitable as an instrument for adjudicating upon the disputes which may arise over whether a business is being run in accordance with the terms of the court’s order.⁸³

The House of Lords’ refusal in *Co-operative Insurance Services v. Argyll Stores Ltd* (1998) to overstretch specific performance in this context seems quite justified. More generally, apart from agreements to transfer land (where specific performance is the

⁷⁸ *Ibid.*

⁷⁹ *Ibid.*

⁸⁰ A. S. Burrows, *Remedies for Torts and Breach of Contract* (3rd edn, Oxford, 2004), 475–81.

⁸¹ [1998] AC 1, 15.

⁸² *Ibid.* (quoting Lord Westbury LC in *Isenberg v. East India House Estate Co. Ltd* (1863) 3 De GJ & S 263, 273).

⁸³ *Ibid.*

primary remedy), English law is right to confine this remedy to a residual role, for these reasons.⁸⁴ First, specific performance is a heavy-handed remedy, sanctioned by contempt of court powers (18.13). It should be narrowly confined, otherwise it threatens to become a remedial sledgehammer. Secondly, the mitigation principle (18.49 in the context of damages, but contrast with respect to debt, 18.05 ff) requires that, in general, an innocent party should be required to act straightaway in order to reduce or even eliminate his loss, and he should not be at liberty to wait for the court to order the guilty party to perform.⁸⁵ Thirdly, the parties can (i) insert liquidated damages clauses or (ii) require payment of a deposit to apply leverage to induce performance (on (i) and (ii), see 19.02 and 19.25).

The last word on the proper scope of specific performance should go to Lord Hoffmann, whose magisterial speech in the *Co-operative Insurance* case (1998) concludes as follows:

From a wider perspective, it cannot be in the public interest for the courts to require someone to carry on business at a loss if there is any plausible alternative by which the other party can be given compensation. It is not only a waste of resources but yokes the parties together in a continuing hostile relationship. The order for specific performance prolongs the battle. If the defendant is ordered to run a business, its conduct becomes the subject of a flow of complaints, solicitors' letters and affidavits. This is wasteful for both parties and the legal system. An award of damages, on the other hand, brings the litigation to an end. The defendant pays damages, the forensic link between them is severed, they go their separate ways and the wounds of conflict can heal.⁸⁶

4. INJUNCTIONS

- 18.20 The general rule is that injunctions are readily awarded to prevent a defendant breaching a 'negative' promise, that is, an undertaking not to do something.⁸⁷ In such a case, an injunction is not subject to the restriction (which governs specific performance) that damages would be an inadequate remedy (18.14). Instead, the courts are willing to grant injunctions to prevent breach of negative undertakings, for example, to enforce restrictive covenants requiring landowners to desist from using the premises for specified purposes (for example, 'the owner will not use, or allow these premises to be used, for the purpose of selling intoxicating liquor'). Burrows suggests that the courts have gone too far in awarding injunctions without inquiring whether damages would be sufficient

84 S. M. Waddams, 'The Choice of Remedy for Breach of Contract', in J. Beatson and D. Friedmann (eds.), *Good Faith and Fault in Contract Law* (Oxford, 1995), 471 ff, provides a compelling defence of the residual role of coercive specific relief.

85 D. Friedmann, 'Economic Aspects of Damages and Specific Performance Compared', in D. Saidov and R. Cunnington (eds.), *Contract Damages: Domestic and International Perspectives* (Oxford, 2008), chapter 2, at 86 ff.

86 *Co-operative Insurance Society Ltd v. Argyll Stores (Holdings) Ltd* [1998] AC 1, 15–16, HL, per Lord Hoffmann.

87 *Doherty v. Allman* (1878) 3 App Cas 709, 720, HL, per Lord Cairns LC.

protection, but he acknowledges that the constant supervision problem and the mitigation issue do not complicate this context.⁸⁸ (As for clauses stipulating that injunctions should be available, Solène Rowan has challenged the view – see the quotations at 18.18 – that the courts will not countenance a usurpation of their discretionary control of this award.)⁸⁹

- 18.21 An injunction can be awarded either to prevent the anticipated wrong ('prohibitory' relief) or to reverse the relevant wrong (a 'mandatory' injunction, for example, following construction on the defendant's land of a fence using materials not complying with the relevant undertaking). However, in the latter situation, where the court is presented with a *fait accompli*, there is a discretion to withhold a mandatory injunction and instead to award damages 'in lieu', that is, as a substitute for the injunction.⁹⁰ For example, when the relevant undertaking requires construction using building material 'X', and instead material 'Y' has been wrongly used, the court would be highly disinclined to make an order to demolish and reconstruct the offending structure.
- 18.22 Just as specific performance will not be granted to compel direct performance of such an obligation (18.17), so, consistently, equity will refuse to use its coercive machinery if the indirect effect will be to apply such compulsion. For example, if a defendant actor, manager, employee, or sportsman has agreed not to work for anyone other than the claimant for a specified period, an injunction to enforce this negative undertaking might indirectly impose compulsion on the defendant to work for, or with, the claimant. 'Indirect compulsion' would arise whenever a defendant might feel the need to continue to advance her brilliant career and so avoid a significant period during which that career would be placed 'on hold' in order to comply with the injunction. Indirect compulsion would in fact arise whenever, more mundanely, the defendant needs to maintain her standard of living.⁹¹ Consistent respect is shown, therefore, to the liberal principle that a person should not be forced to perform 'personal services' against his will. Thus, in *Warren v. Mendy* (1989), the claimant, a boxing manager, sought an injunction to restrain the defendant from interfering with a management contract between him and Benn, a talented young boxer (the so-called 'economic torts' protect the claimant's interest in restraining a third party from inducing breach of a contract, or from interfering with its performance: 17.69).⁹²

88 A. S. Burrows, *Remedies for Torts and Breach of Contract* (3rd edn, Oxford, 2004), 527–9.

89 S. Rowan, 'For the Recognition of Remedial Terms Agreed Inter Partes' (2010) 126 LQR 448, 449–55, 470–5.

90 E.g. *Oxy-Electric Ltd v. Zaiduddin* [1991] 1 WLR 115, Hoffmann J (application for striking out refused; case to proceed to trial); *Jaggard v. Sawyer* [1995] 1 WLR 269, CA (injunction refused; damages in lieu awarded under section 50 of the Senior Courts Act 1981).

91 *Warren v. Mendy* [1989] 1 WLR 853, CA, noted by H. McLean, [1990] CLJ 28, noting *Lumley v. Wagner* (1852) 1 De GM & G 604, and *Warner Bros Pictures Inc. v. Nelson* [1937] 1 KB 209, and *Page One Record Ltd v. Britton* [1968] 1 WLR 157 ('The Troggs' case); Mance LJ in *LauritzenCool AB v. Lady Navigation Inc.* [2005] EWCA Civ 579; [2006] All ER 866, CA (18.22); P. Saprai, 'The Principle against Self-Enslavement in Contract Law' (2009) 25 *Journal of Contract Law* 26.

92 [1989] 1 WLR 853, CA.

The Court of Appeal held that no injunction against the third party should be granted because the practical effect would be that Benn, the *contracting* party, would be indirectly compelled to continue to serve under the claimant's management. This was because Benn, as a highly paid boxer, in a notoriously short sporting career, did not have the practical choice of 'stacking supermarket shelves' as an alternative source of income. Nourse LJ explained the modern approach as follows:⁹³

The difficulty ... is that the human necessity of maintaining the skill or talent may practically bind the servant to the contract, compelling him to perform it.

He added:⁹⁴

Compulsion is a question to be decided on the facts of each case, with a realistic regard for the probable reaction of an injunction on the psychological and material, and sometimes the physical, need of the servant to maintain the skill or talent. The longer the term for which an injunction is sought, the more readily will compulsion be inferred.

But, as the Court of Appeal in the *LauritzenCool* case (2006) acknowledged, the liberal principle that *individuals* should not be compelled (directly or indirectly) to work for others does not apply if the defendant is a company. In the *LauritzenCool* case, the court held that it was legitimate to issue an injunction to prevent a company from removing its two ships from the charterer. Mance LJ said:

[N]either the fact that the contracts ... were for services in the form of a time charter nor the existence ... of a fiduciary⁹⁵ relationship of mutual trust and confidence represents in law any necessary or general objection in principle to the grant of injunctive relief precluding the [owners] from employing their vessels [in a way contrary to the charterparty] pending the outcome of the current arbitration. Nor does it afford any such objection to ... such relief that the only realistic commercial course ... left to the [owners] was ... to provide the vessels ... and to perform the charters.⁹⁶

In *Regent International Hotels (UK) Ltd v. Pageguide Ltd* (1985)⁹⁷ (cited with approval in the *LauritzenCool* case), Ackner LJ contrasted a personal relationship between a pop group and a manager (where an injunction would be inappropriate)⁹⁸ and the commercial context of a company's undertaking to manage a hotel (where an injunction would be appropriate, as in the *Regent International Hotel* case itself).

⁹³ *Ibid.*, at 857.

⁹⁴ *Ibid.*, at 867.

⁹⁵ *Calvert v. William Hill Credit Ltd* [2008] EWCA Civ 1427; [2009] Ch 330, at [53]; *Parker and Mellows: The Modern Law of Trusts* (9th edn, London, 2008), 10-048 ff; J. Edelman, 'When Do Fiduciary Duties Arise?' (2010) 126 LQR 302.

⁹⁶ *LauritzenCool AB v. Lady Navigation Inc.* [2005] EWCA Civ 579; [2006] All ER 866, CA, at [30].

⁹⁷ *The Times*, 13 May 1985, CA.

⁹⁸ *Page One Record Ltd v. Britton* [1968] 1 WLR 157.

5. DAMAGES⁹⁹

18.23 *Outline of main points.* The main points of this topic are as follows:

- (1) *Agreed compensation.* In advance of breach, the parties can agree upon the measure of damages which the innocent party will receive in the event of breach. But the courts will not uphold these stipulations if they are punitive, that is, wholly disproportionate (see the discussion of the ‘penalty doctrine’ at 19.02).
- (2) *Nominal damages.* For any breach of contract, a claimant is entitled to nominal damages. This is a token sum signifying the fact that there has been a technical legal wrong (sums of £5 or £10, for example).¹⁰⁰
- (3) *Substantial damages.* If the claimant seeks substantial damages, that is compensation for real loss, rather than the token award of nominal damages, ‘the claimant must prove, on a balance of probabilities, [recognised] loss resulting from the breach of contract’.¹⁰¹ Substantial damages can be awarded only if the claimant shows a recognised type of loss, such as economic loss, personal injury or damage to property.¹⁰² If no loss can be shown, the claimant is entitled only to nominal damages, since to award more than that token amount would be to punish the defendant. As Lord Lloyd of Berwick said in *Ruxley Electronics and Construction Ltd v. Forsyth* (1996), ‘If he has suffered no loss, as sometimes happens, he can recover no more than nominal damages. The object of damages is always to compensate the plaintiff, not to punish the defendant.’¹⁰³ There is also a restriction against making damages awards for wholly ‘speculative loss’ (18.33).
- (4) *True compensation.* The compensatory aim necessarily precludes double compensation or over-compensation for the same loss (and thus damages should reflect the fact that the claimant would have paid tax on the sums which the compensation is intended to replace).¹⁰⁴
- (5) *Protection of expectations and indemnification of reliance loss.*
 - (a) The main aim of compensatory damages is to place the promisee in the position he would have been in if the contract had been properly performed. This is the so-called ‘expectation’ or ‘loss of bargain’ measure (18.25). As Parke B said in *Robinson v. Harman* (1848), the main aim of contractual damages is to place the

99 *McGregor on Damages* (18th edn, London, 2009) is the leading work; other important studies are: A. S. Burrows, *Remedies for Torts and Breach of Contract* (3rd edn, Oxford, 2004); A. Tettenborn (with D. Wilby and D. Bennett), *The Law of Damages* (London, 2003), chapter 6, at 127 ff, and chapter 19.

100 *McGregor on Damages* (18th edn, London, 2009), chapter 10.

101 *Bank of Credit & Commerce International SA (in liquidation) v. Ali (No. 2)* [2002] EWCA Civ 82; [2002] 3 All ER 750; [2002] ICR 1258; [2002] IRLR 460, at [14], *per* Pill LJ.

102 E.g. limits upon damages for disappointment (*Farley v. Skinner* [2001] UKHL 49; [2002] 2 AC 732, HL, noted at 18.43 below); contractual damages are unavailable for damage to reputation except in special situations: A. Burrows, in A. Burrows (ed.), *English Private Law* (2nd edn, Oxford, 2007), 21.48 ff, for exceptions.

103 [1996] 1 AC 344, 365, HL.

104 A. S. Burrows, *Remedies for Torts and Breach of Contract* (3rd edn, Oxford, 2004), 199 ff (noting *British Transport Commission v. Gourley* [1956] AC 185, HL, and associated cases).

claimant (the promisee) in the position he would have been in if the promise had been performed or the warranty had been accurate.¹⁰⁵

- (b) A subsidiary type of damages is to restore the claimant monetarily to the position he enjoyed before the contract was breached, the so-called 'reliance loss' measure (18.25, 18.26).
- (6) *Damages are to compensate for loss rather than to disgorge the defendant's gain.* The general function of damages is to compensate rather than to prevent the defendant's unjust enrichment. However, the House of Lords in *Attorney-General v. Blake* (2001)¹⁰⁶ recognised that the courts can make an exceptional and discretionary award, known as an equitable account, to strip a defendant of a gain made as a result of breach of contract (see further 18.57 ff).
- (7) *Compensation is not punishment.* Contractual damages are intended to compensate the claimant, rather than to punish the defendant.¹⁰⁷
- (8) *Damages are generally assessed at the date of breach.* In general,¹⁰⁸ damages are assessed with regard to the facts as they subsisted at the time of breach,¹⁰⁹ notably in the cases of failure to accept or to deliver goods in contracts of sale.¹¹⁰ However, a large exception to this proposition was introduced by the House of Lords in '*The Golden Victory*' (2007),¹¹¹ where facts subsequent to the breach were shown to have inevitably reduced the value of the damages claim.

105 (1848) 1 Exch 850, 855; on the claimant's expectation or performance interest, Fuller and Perdue, 'The Reliance Interest in Contract Damages' (1936) 46 *Yale Law Journal* 52 and 373 (in two parts); D. Friedmann, 'The Performance Interest in Contract Damages' (1995) 111 LQR 628; D. Friedmann, 'A Comment on Fuller and Perdue' (2001) 1 *Issues in Legal Scholarship* 11; P. Jaffey, 'Damages and the Protection of Contractual Reliance', in D. Saidov and R. Cunnington (eds.), *Contract Damages: Domestic and International Perspectives* (Oxford, 2008), chapter 6; R. Stevens, 'Damages and the Right to Performance ...', in J. W. Neyers, R. Brounagh and S. G. A. Pitel (eds.), *Exploring Contract Law* (Oxford, 2009), 171 ff; C. Webb, 'Justifying Damages', in J. W. Neyers, R. Brounagh and S. G. A. Pitel (eds.), *Exploring Contract Law* (Oxford, 2009), 139 ff; D. Pearce and R. Halson, 'Damages for Breach of Contract: Compensation, Restitution, and Vindication' (2008) 28 OJLS 73–98.

106 [2001] 1 AC 268, HL.

107 *Addis v. Gramophone Co. Ltd* [1909] AC 488, HL; *McGregor on Damages* (18th edn, London, 2009), 11–016; otherwise in Canada, *Royal Bank of Canada v. Got* (2000) 17 DLR (4th) 385 (Supreme Court of Canada), noted by J. Edelman, (2001) 117 LQR 539; *Whiten v. Pilot Insurance Co.* [2002] SCC 18; [2002] 1 SCR 595 (Supreme Court of Canada); *Honda Canada Inc. v. Keays* [2008] SCC 39; (2008) 294 DLR (4th) 371 (Supreme Court of Canada), noted by M. McInnes, (2009) 125 LQR 16, at 19–20; as for punitive damages in English tort law, see *Kuddus v. Chief Constable of Leicestershire* [2002] 2 AC 122, HL, and *A v. Bottrill* [2003] 1 AC 449, PC.

108 Cf Lord Wilberforce in *Johnson v. Agnew* [1980] 367, 401, HL: 'not an absolute rule ... the court has power to fix such other date as may be appropriate.'

109 S. Waddams, 'The Date for the Assessment of Damages' (1981) 97 LQR 445–61.

110 Respectively, sections 50(3) and 51(3) of the Sale of Goods Act 1979.

111 '*The Golden Victory*' [2007] UKHL 12; [2007] 2 AC 353; M. Furmston, 'Actual Damages, Notional Damages and Loss of a Chance', in D. Saidov and R. Cunnington (eds.), *Contract Damages: Domestic and International Perspectives* (Oxford, 2008), 419, at 424 ff; D. McLaughlan, 'Expectation Damages: Avoided Loss, Offsetting Gains and Subsequent Events', in D. Saidov and R. Cunnington (eds.), *Contract Damages: Domestic and International Perspectives* (Oxford, 2008), chapter 15; C. J. Morgan, [2007] CLJ 263; C. Nicholls, [2008] JBL 91; B. Coote, (2007) 123 LQR 503; M. Mustill, (2008) 124 LQR 569–85; Sir Bernard Rix, 'Lord Bingham's Contributions to Commercial Law', in M. Andenas and D. Fairgrieve (eds.), *Tom Bingham and the Transformation of the Law: A Liber Amicorum* (Oxford, 2009), at 679–83; earlier, S. Waddams, 'The Date for the Assessment of Damages' (1981) 97 LQR 445.

- (9) *Finality*. A claimant cannot obtain damages in successive actions in respect of the same cause of action: 'Damages resulting from one and the same cause of action must be assessed and recovered once and for all.'¹¹²
- (10) *Limiting factors*. Damages are subject to various doctrines intended to prevent unjust or excessive recovery by the claimant:
- (a) *Causation*. Damages for a loss cannot be recovered if there is no sufficient causal connection between the defendant's breach and that loss (18.39).
 - (b) *Remoteness*. The loss must also be within the bounds of the 'remoteness' test. A type of loss is not too remote if, objectively, it is reasonable to suppose that the parties would have envisaged it as a serious or real possibility; or the type of loss was in fact contemplated as a serious or real possibility, because there is evidence that the defendant had special knowledge of this matter at the date of contracting, especially if that knowledge has been specifically notified to him by the other party (18.40).
 - (c) *Mitigation*. Damages cannot be recovered to the extent that the claimant, after suffering a breach of contract, has unreasonably brought the loss upon himself or failed to avert or limit it; in either situation, the claimant will have 'failed to mitigate his loss' (18.49).
 - (d) *Contributory negligence (narrow compass)*. Some contractual damages claims can be reduced on the basis of the claimant's contributory negligence (see below). However, in the field of contract law, this defence applies only if (i) the relevant contractual duty is one to exercise reasonable care; and (ii) this contractual duty subsists concurrently with a tortious obligation to exercise such care (18.50).
 - (e) *'Impecuniosity'*. As Burrows notes, a claimant cannot be prevented from recovering loss merely because that loss stems from his lack of funds or 'impecuniosity'; although the *Liesbosch* case (1933), which enunciated this principle, has not been formally overruled, the case is now largely treated as bad law.¹¹³
 - (f) *Litigation costs and damages*. As Louise Merrett has shown,¹¹⁴ the costs incurred in bringing or defending a claim against the other party are recoverable only under the costs regime of the procedural rules (notably CPR Part 44);¹¹⁵ there is,

112 *Brunsdon v. Humphrey* (1884) 14 QBD 141, 147, CA, *per* Bowen LJ; *Republic of India v. India Steamship Co. Ltd ('The Indian Grace')* [1993] AC 410, 420–1, HL; L. A. Collins, (1992) 108 LQR 393, 394; *Jaggard v. Sawyer* [1995] 1 WLR 269, 284, CA; *Deeny v. Gooda Walker Ltd* [1995] 1 WLR 1206, 1214; G. Spencer Bower, A. K. Turner and K. R. Handley, *The Doctrine of Res Judicata* (3rd edn, London, 1996), chapter 21; N. Andrews, *English Civil Procedure* (Oxford, 2003), 40.12 n. 28; A. S. Burrows, *Remedies for Torts and Breach of Contract* (3rd edn, Oxford, 2004), 174 ff.

113 *McGregor on Damages* (18th edn, London, 2009), 6–108 ff, noting the rejection in *Lagden v. O'Connor* [2004] 1 AC 1067, at [62], of *Liesbosch v. Owners of the Steamship Edison ('The Edison')* [1933] AC 449, HL.

114 L. Merrett, 'Costs as Damages' (2009) 125 LQR 468.

115 Generally on costs, see N. Andrews, 'Costs and Conditional Fee Agreements in English Civil Litigation', in P. Gottwald (ed.), *Litigation in England and Germany: Legal Professional Services, Key Features and Funding* (Bielefeld, 2010), 185–216; N. Andrews, *Contracts and English Dispute Resolution* (Tokyo, 2010), chapter 19; N. Andrews, *The Modern Civil Process* (Tübingen, 2008), chapter 9; N. Andrews, *English Civil Procedure* (Oxford, 2003), chapters 35 to 37; M. J. Cook, *Cook on Costs* (London, annual editions); P. Hurst, *Civil Costs* (4th edn, London, 2007); A. Zuckerman, *Civil Procedure* (2nd edn,

in general, no scope to recoup such expenses as contractual compensation.¹¹⁶ However, as Merrett has also shown, damages can be awarded in favour of A (i) where A's contractual claim against B concerns a breach which led to A incurring litigation expenses *vis-à-vis* a third party;¹¹⁷ or (ii) when B's breach led A to incur litigation costs in a *foreign jurisdiction*.¹¹⁸

(g) *Defendant's choice or discretion in performing contract: assessment of damages when defendant in breach.* *Durham Tees Valley Airport Ltd v. bmibaby Ltd* (2010)¹¹⁹ has confirmed the following propositions.

- (i) Damages will not be awarded if the claimant is not entitled to recover compensation in respect of benefits which the defendant was not legally obliged to confer.
- (ii) However, where it is clear that the claimant has suffered loss in respect of a legally protected right, but the defendant had a choice between two or more ways to perform, the claimant will be awarded damages on the less or least onerous basis, tilting matters in favour of the defendant.
- (iii) Where, however, the defendant's performance involves a single obligation, within which he enjoys elements of discretion, the courts are prepared to regulate this by reference to standards of reasonableness, where necessary and appropriate.

In the *Durham* case (2010) (for this case's facts, see 4.07) the Court of Appeal examined the matters summarised here as (i) to (iii). Patten LJ said:¹²⁰

The court has to look at the relevant economic and other surrounding circumstances to decide on the level of performance which the defendant would have adopted. The judge conducting the assessment must assume that the defendant would not have acted outside the terms of the contract and would have performed it in his own interests having regard to the relevant factors prevailing at the time. But the court is not required to make assumptions that the defaulting party would have acted uncommercially merely in order to spite the claimant.

London, 2006), chapter 26; Sir Rupert Jackson, *Review of Civil Litigation Costs* (London, 2010), on which see A. A. S. Zuckerman, 'The Jackson Final Report on Costs – Plastering the Cracks to Shore Up a Dysfunctional System' (2010) 29 *Civil Justice Quarterly* 263.

116 This rule applies whether the claim is for damages in contract or tort: leading authorities were reviewed by Devlin LJ in *Berry v. British Transport Commission* [1962] 1 QB 306, 320–2, CA.

117 E.g. *British Racing Drivers Club v. Hextall Erskine & Co.* [1996] BCC 727, Carnwath J.

118 E.g. *Union Discount Co. Ltd v. Zoller* [2001] EWCA Civ 1755; [2002] 1 WLR 1517.

119 [2010] EWCA Civ 485.

120 *Ibid.*, at [79], *per* Patten LJ (Toulson and Mummery LJ agreed: [147] and [150]), considering, notably, *Abrahams v. Herbert Reisch Ltd* [1922] 1 KB 477, CA (preferring the approach of Atkin LJ to that of Scrutton LJ); *Lavarack v. Woods of Colchester* [1967] 1 QB 278, CA; *Paula Lee Ltd v. Zehil & Co. Ltd* [1983] 2 All ER 390, Mustill J; *Kurt A Becher GmbH & Co. KG v. Roplak Enterprises SA* ('*The World Navigator*') [1991] 2 Lloyd's Rep 23, CA; *Cantor Fitzgerald International v. Horkulak* [2004] EWCA Civ 1287; [2005] ICR 402.

18.24 *Types of money claims.* A threefold distinction is drawn when examining the aim of various contractual money claims (notably claims for compensation, but also restitutionary actions in the contractual context). This distinction involves three economic ‘interests’ that the claimant might wish to protect:¹²¹

- (1) ‘the expectation interest’ (loss of profit/deprivation of gain; loss of income due to damage to property or personal injury) (see further 18.25 below);
- (2) ‘the reliance interest’ (money wasted on the project; property damage; some forms of personal injury loss) (on this see 18.25 and 18.26); or
- (3) ‘the restitutionary interest’ (18.51 ff):
 - (a) claims for money had and received, or recompense for goods supplied or services rendered;
 - (b) claims for recovery of payments based on failure of consideration;
 - (c) profit-stripping claim based on equitable remedy of account.

Of these, it should be noted that only (c) requires proof of a breach of contract; categories (a) and (b) arise without the need to show any breach of contract; indeed, it is often necessary to invoke categories (a) and (b) precisely because no contract has arisen, or it was invalid at its inception.

Types of damages claims

18.25 *Expectation and reliance loss claims.* The law distinguishes ‘expectation’ and ‘reliance’ damages for breach of contract. The former measure of damages aims to place the claimant in the economic position which he would have enjoyed had the defendant not breached the contract. This forward-looking measure of compensation protects the promisee’s interest in making a gain under a profitable contract. In the absence of a successful claim for loss of profit or expectation damages, the default form of compensation is ‘reliance damages’. This concerns the claimant’s ‘out-of-pocket’ expenditure incurred when attempting to perform his side of the contract. Claims for wasted expenditure arise where the claimant cannot prove lost profits, or such a claim is too difficult to quantify. This was the position in *Anglia Television Ltd v. Reed* (1972), where the defendant actor failed to participate in filming, but the claimant company could not show that its intended film would have been profitable.¹²² The Court of Appeal awarded compensation for the expenses wasted when the project had to be scrapped, and the award also covered pre-contractual expenditure made in contemplation of the filming. It is not possible for an award of damages to involve satisfaction of both reliance and loss of bargain claims

¹²¹ Following Fuller and Perdue, ‘The Reliance Interest in Contract Damages’ (1936) 46 *Yale Law Journal* 52 and 373 (in two parts); the analysis underlies Steyn LJ’s comment in *Surrey County Council v. Bredero Homes Ltd* [1993] 1 WLR 1361, 1369B–G, CA; D. Friedmann, ‘The Performance Interest in Contract Damages’ (1995) 111 LQR 628; D. Friedmann, ‘A Comment on Fuller and Perdue’ (2001) 1 *Issues in Legal Scholarship* 11; P. Jaffey, ‘Damages and the Protection of Contractual Reliance’, in D. Saidov and R. Cunnington (eds.), *Contract Damages: Domestic and International Perspectives* (Oxford, 2008), chapter 6.

¹²² [1972] 1 QB 60, CA.

if this will involve the claimant recovering twice for the same tranche of loss. So a claim for gross profits must be reduced to account for the claimant's expenditure in realising those profits. In short, only net profits are recoverable.

18.26 There is an important limit on the reliance loss claim. The defendant might show that the claimant had no chance of 'covering his expenses' even if the contract had not been breached; in other words, that the contract was inherently loss-making for the innocent party.¹²³ This can be justified for two reasons: first, as a matter of causation, because the claimant would have been impoverished by the contract even if everything had been performed perfectly, and so he suffered no loss as a result of the breach;¹²⁴ and, secondly, otherwise an award of substantial damages would be punitive. In such a case, the defendant need only pay non-compensatory 'nominal damages', signifying his bare and technical breach.

18.27 *Nature of 'cost of cure' (or 'reinstatement') damages.*¹²⁵ The 'cost of cure' or reinstatement measure of damages concerns the cost, normally the hire of third party services, of putting right defective work or finishing an incomplete job of work. Some have linked this measure of compensation with the broader concept of a so-called 'performance interest' in contract law: that the innocent party should be enabled to receive as nearly as practicable what he bargained for.¹²⁶ However, it is submitted that this idea should not become an unruly horse because cost of cure damages often exceed the diminution in value of the relevant subject matter. For example, it might cost £10,000 to build a wall in a garden, but failure to build the wall might hardly reduce the property's market value, perhaps not even at all. The court will need to make a broad assessment to determine whether the extra cost is justified and whether the claimant can show a special need for the promised result. Oliver J's discussion of this issue in *Radford v. De Froberville* (1977) is especially helpful (see 18.28).¹²⁷ The cost of cure measure is inappropriate if it will result in a windfall for the claimant, exceeding his real loss, or if the proposed remedial work is disproportionate and even wasteful. Of course, if the cost of cure measure will rectify the breach more cheaply than an award of damages measured by the subject matter's diminution in market value, the courts will award the cost of cure measure, because this is consistent with the defendant's duty to mitigate (18.49).¹²⁸ Solène Rowan has contended that the

123 *C & P Haulage v. Middleton* [1983] 1 WLR 1461, CA.

124 *CCC Films v. Impact Quadrant Ltd* [1985] QB 16, Hutchison J.

125 D. Harris, A. Ogus and J. Phillips, 'Contract Remedies and the Consumer Surplus' (1979) 95 LQR 581; D. Pearce and R. Halson, 'Damages for Breach of Contract: Compensation, Restitution, and Vindication' (2008) 28 OJLS 73, 82, 91–3.

126 *Panatown* [2001] 1 AC 518, 548–53, 585–92, HL, *per* Lords Millett and Goff (on this case, see 7.27); for a denial that there is a strong right to *actual performance* of the contract, see F. M. B. Reynolds, in P. Finn (ed.), *Essays on Contract* (Sydney, 1987)).

127 [1977] 1 WLR 1262, Oliver J; and, for Australian discussion, see *Tabcorp Holdings Ltd v. Bowen Investments Pty Ltd* [2009] HCA 8; (2009) ALJR 390 (cost of cure damages for tenant's breach of a no-alteration clause).

128 *Ruxley Electronics and Construction Ltd v. Forsyth* [1996] 1 AC 344, 366D, HL, *per* Lord Lloyd.

courts should be prepared to uphold a clause stipulating that the cost of cure measure should be available to the innocent party.¹²⁹

- 18.28** *Cost of cure claim upheld.* Oliver J awarded the cost of cure measure in *Radford v. De Froberville* (1977):¹³⁰

The claimant sold part of his land to the defendant, who promised to construct a wall (made of brick, and seven foot high) on his portion of land to partition the two resulting plots. The defendant failed to build the wall. But the claimant could not bring specific performance to compel him to build the wall because the relevant plot had been sold on by the defendant to a third party. The defendant argued that damages for his admitted default should be confined to the trivial amount by which the absence of a wall reduced the value of the claimant's land. If adopted, the compensatory damages would be nominal. Instead, the claimant sought the much larger amount necessary to construct the wall (on the claimant's side of the land). That would cost £3,400 at the time of trial. Oliver J was satisfied both that the claimant seriously intended to use the cost of cure award to pay for construction of a wall and that this award was otherwise justified.¹³¹ Furthermore, the sum should be calculated at trial prices rather than the lower prices prevailing at the time of the breach in the mid-1960s (when the wall could have been built for only £1,200).¹³²

- 18.29** *Cost of cure claim rejected.* Megarry V-C refused to award the cost of cure measure in *Tito v. Waddell (No. 2)* (1977) because the money would not have been spent to rectify the breach.¹³³

The claimants were a group of displaced islanders. They owned land on a Pacific island where the defendant had mined phosphate under a long-standing licence. The agreement required the defendant, after it had extracted the minerals, to refurbish the worked-out land, re-planting trees and shrubs. The defendant failed to do this. Megarry V-C declined to award the claimant the cost of the defendant's promised rehabilitation of the island.¹³⁴ The islanders now lived on another island 1,500 miles away. Megarry V-C considered that they had no real interest in spending the money on refurbishing the island. The claimants were instead restricted to the amount of the diminution in the land's value as a result of the default. This loss of value measure would enable them, if they wished, to make a 'cosmetic'

129 S. Rowan, 'For the Recognition of Remedial Terms Agreed Inter Partes' (2010) 126 LQR 448, 455–7.

130 [1977] 1 WLR 1262, 1268–88, Oliver J; D. Harris, A. Ogus and J. Phillips, (1979) 95 LQR 581, at 581–2, 590; G. H. Jones, (1983) 99 LQR 443, 450; H. Beale, in P. B. H. Birks (ed.), *Wrongs and Remedies in the Twenty-First Century* (Oxford, 1996), 231.

131 [1977] 1 WLR 1262, 1284E.

132 *Ibid.*, at 1267H.

133 [1977] Ch 106, 328, *per* Megarry V-C.

134 *Ibid.*, at 336D.

rehabilitation of the island.¹³⁵ The judge also rejected the claim for specific performance (on which see 18.14 ff) as 'absurd' since 'the time and the cost would be very great, and wholly disproportionate to the meagre and long-delayed benefit that might in the end be achieved'.¹³⁶ It would involve planting coconut trees, reaching maturity only twenty years later.

The House of Lords in *Ruxley Electronics and Construction Ltd v. Forsyth* (1996)¹³⁷ refused the cost of cure measure because the claimant was merely using this as a vindictive claim, and because expensive remedial work would be disproportionate to the claimant's objective loss of enjoyment.

X hired Y to build a swimming pool in his garden. The pool was constructed 18 inches shallower than specified. The action began as a claim by the swimming pool builder who was still owed some money for the job. The customer counter-claimed for cost of cure damages so that he could have the pool entirely reconstructed to render it deep enough to comply with the agreed depth. In fact, the contractor had already reconstructed the pool once, after it had developed a crack. It was clear that the customer was clutching at every conceivable opportunity to augment the damages owed by the contractor. For the contractor, this had become the contract from hell. The trial judge considered that the customer had no real intention of reconstructing the pool. He held (1) that 'flat' diving was still safe, even taking account of the fact that X was quite tall; (2) that there was no market diminution of value. He refused the cost of cure measure, the expense of deepening the pool, which would require £21,560, and instead awarded £2,500 for loss of amenity (a claim for intangible loss). The fact that this was a suggested 'second time' reconstruction is mentioned in Lord Lloyd's speech¹³⁸ (on the same point, see also Staughton LJ in the Court of Appeal).¹³⁹ A majority of the Court of Appeal, rather censoriously, substituted the cost of cure measure.¹⁴⁰ Otherwise, they said, X would be denied an aspect of the bargain which he had paid for. But the House of Lords, agreeing with the trial judge, held that the cost of cure measure was 'unreasonable' and 'disproportionate' on these facts. The House of Lords restored the award of £2,500 for loss of amenity. Lord Jauncey said:¹⁴¹

Damages are designed to compensate for an established loss and not to provide a gratuitous benefit to the aggrieved party from which it follows that the reasonableness of an award of damages is to be linked directly to the loss sustained. If it is unreasonable in a particular case to award the cost of reinstatement it must be because the loss sustained does not extend to the need to reinstate.

135 *Ibid.*, at 341–342A; American authorities cited by G. H. Jones, (1983) 99 LQR 443, 448–9.

136 [1977] Ch 106, 328.

137 [1996] 1 AC 344, 366C, HL.

138 *Ibid.*, at 362.

139 [1994] 1 WLR 650, 652, CA.

140 Staughton and Mann LJJ, with Dillon LJ dissenting.

141 [1996] 1 AC 344, 357, HL.

And Lord Lloyd of Berwick, having cited Cardozo J in the Court of Appeals of New York in *Jacob & Youngs v. Kent* (1921),¹⁴² said:¹⁴³

Cardozo J's judgment is important, because it establishes two principles, which I believe to be correct, and which are directly relevant to the present case; first, the cost of reinstatement is not the appropriate measure of damages if the expenditure would be out of all proportion to the benefit to be obtained, and, secondly, the appropriate measure of damages in such a case is the difference in value, even though it would result in a nominal award.

The *Ruxley* case is a rather unusual building case. The defect in performance was relatively trivial, but the cost of rectification was high. Furthermore, the relations between the parties had manifestly become very sour. And the contractor had already rebuilt the pool entirely to remedy a crack. Against this background, it is clear that the House of Lords did not intend to subvert the general approach that the general measure in building cases is nevertheless the cost of cure¹⁴⁴ (as *Iggleden v. Fairview New Homes (Shooters Hill) Ltd* (2007) illustrates).¹⁴⁵ Indeed, the House of Lords expressly approved the relevant supporting authorities.

As for the final award of £2,500 (the quantification of which was not the subject of the final appeal), Lord Mustill said that this vindicated the innocent party's 'consumer surplus', that is, damages aimed at reflecting legitimate consumer dissatisfaction in the absence of objective market-price diminution in value.¹⁴⁶ Lord Mustill was attracted by the academic discussion of this concept. He said:¹⁴⁷

[T]he law must cater for those occasions where the value of the promise to the promisee exceeds the financial enhancement of his position which full performance will secure. This excess, often referred to in the literature as the 'consumer surplus', is usually incapable of precise valuation in terms of money, precisely because it represents a personal, subjective and non-monetary gain. Nevertheless, when it exists the law should recognise it and compensate the promisee.

But, more cautiously, Lord Lloyd preferred to treat this award as an instance of disappointment damages.¹⁴⁸

A similar struggle to find a middle way between an award on the cost of cure measure and nominal damages is discernible in *Freeman v. Niroomand* (1996), where the Court of Appeal upheld an award of £130 against a builder who had failed to build a porch to the claimant's house according to the contractual specification.¹⁴⁹ No diminution in the

142 129 NE 889 (NY Court of Appeals, 1921).

143 [1996] 1 AC 344, 366, HL.

144 *East Ham Corporation v. Bernard Sunley & Sons Ltd* [1966] AC 406, HL, and *Linden Gardens Trust Ltd v. Lenesta Sludge Disposals Ltd* [1994] 1 AC 85, 110G, HL, *per* Lord Browne-Wilkinson (generally on that case, see 7.26).

145 [2007] EWHC 1573 (TCC), Coulson J.

146 E.g. the 'bad holiday' cases: *Jarvis v. Swan Tours Ltd* [1973] QB 233, CA, *Jackson v. Horizon Holidays Ltd* [1975] 1 WLR 1468, CA.

147 *Ibid.*, at 360, citing D. Harris, A. Ogus and J. Phillips, 'Contract Remedies and the Consumer Surplus' (1979) 95 LQR 581 (also cited by Lord Millett in the *Panatown* case, [2001] 1 AC 518, 589).

148 *Ruxley Electronics and Construction Ltd v. Forsyth* [1996] 1 AC 344, 374, HL.

149 (1996) 52 Con LR 116, CA.

property's value resulted from this shortcoming. Millett LJ said that the trial judge had measured the loss as 'the amount which the builder had saved by not providing a porch in accordance with the contractual specifications'.¹⁵⁰ McGregor suggests¹⁵¹ that the award might be interpreted 'as an early manifestation of the new restitutionary damages' or as 'damages for non-pecuniary loss along the "consumer surplus" lines that Lord Mustill outlined in the *Ruxley* case' (see above).

18.30 *Danger of 'windfall' damages.* If the work has already been done, this problem does not arise.¹⁵² Instead, the question is whether the expenditure was consistent with the duty to mitigate (18.49). But, if no remedial work has been undertaken, should it matter that the claimant has no real intention to use the cost of cure damages to carry out remedial works?¹⁵³ If there is no clear intention to spend the money, the court should not make this award. Conversely, if the innocent party has a genuine and fixed intention to devote the money to rectifying the default¹⁵⁴ (perhaps, as in the *Ruxley* case, by offering a formal undertaking to spend the money on repairs), this will be a relevant factor, but not a decisive one, in favour of ordering the reinstatement measure.¹⁵⁵ In the *Ruxley* case, the reinstatement award would not have been a reasonable award, given the absence of any significant loss caused by the 18-inch shortfall in the construction of the pool at its deep end. The trial judge had found as a fact that the customer could still safely carry out shallow diving into the pool. Lords Jauncey and Lloyd said that the customer's (tactical) willingness to give an undertaking to spend the cost of cure damages on repairs had made no difference,¹⁵⁶ because the trial judge had found that the customer had no real intention of rebuilding the pool.¹⁵⁷ And so that party's willingness now to offer such an undertaking was transparently an attempt to obtain a substantial award of damages for vindictive purposes. This runs counter to the compensatory aim: for the innocent party 'cannot be allowed to create a loss, which does not exist, in order to punish the defendants for breach of contract'.¹⁵⁸

18.31 In *Sunrock Aircraft Corp. v. Scandinavian Airlines Systems* (2007), the Court of Appeal applied the *Ruxley* case's principles.¹⁵⁹ The defendant had breached an aircraft lease by failing to repair 'scab patches' on its fuselage. The claimant had later sold the aircraft to

¹⁵⁰ *Ibid.*, at 121.

¹⁵¹ *McGregor on Damages* (18th edn, London, 2009), 26-014.

¹⁵² *Tito v. Waddell* (No. 2) [1977] Ch 106, 333A, citing *Jones v. Herxheimer* [1950] 2 KB 106.

¹⁵³ *Radford v. De Froberville* [1977] 1 WLR 1262, 1270E, per Oliver J (claimant's wish to spend the money was clear: see *ibid.*, at 1282); *Wigsell v. School for the Indigent Blind* (1882) 8 QBD 357 (Cave and Field JJ, Divisional Court); in *Tito v. Waddell* (No. 2) [1977] 106, 333, per Megarry V-C.

¹⁵⁴ *Tito v. Waddell* (No. 2) [1977] Ch 106, 333-4, 336, discussing the so-called 'indicia of serious intent'; *Wigsell v. School for the Indigent Blind* (1882) 8 QBD 357, 363-4; *Radford v. De Froberville* [1977] 1 WLR 1262, 1282, per Oliver J.

¹⁵⁵ [1996] 1 AC 344, 373 HL, per Lord Lloyd.

¹⁵⁶ *Ibid.*, at 359C, 373E.

¹⁵⁷ *Ibid.*, at 372H.

¹⁵⁸ *Ibid.*, at 373E.

¹⁵⁹ [2007] EWCA Civ 882; [2007] 2 Lloyd's Rep 612.

a third party, but had suffered no loss due to the patches. The Court of Appeal upheld the trial judge's award of nominal damages for this breach. Thomas LJ explained:¹⁶⁰

[T]he scab patches did not affect the marketability of the aircraft for leasing or its value; that was because in an aircraft of [this] age ... at the time of redelivery, it would be extraordinary not to find scab patches on such an aircraft. It was also clear that there was no point in repairing them as they had no effect on performance or on the value of the aircraft ... It followed therefore that ... Sunrock ... had in fact suffered no loss.

18.32 Finally, the cost of cure measure should not be confused with the question of compensating the claimant for harm *already suffered*, *whether this is economic or physical loss, or loss of amenity*. The Court of Appeal's decision in *Dean v. Ainley* (1987) is perhaps an example of this confusion.¹⁶¹ The defendant vendor had failed to dampproof a cellar, and this had made that room unusable for a long period. Kerr LJ, impressed by this last fact, said that there was no need for the claimant formally to undertake to spend the money on the repairs. His liberal approach seems to have conflated the loss of use (already suffered) and the prospective cost of preventing such damp.

18.33 *Loss of chance claims and the problem of speculative loss*. This is the problem of 'speculative loss'. In *Allied Maples Group v. Simmons & Simmons* (1995),¹⁶² the leading modern contract case on this topic, the Court of Appeal held that there can be no recovery in respect of a lost chance if the likelihood of its occurrence cannot be regarded as 'realistic' or 'substantial'. Stuart-Smith LJ said:¹⁶³

[T]he plaintiff must prove as a matter of causation that he has a real or substantial chance as opposed to a speculative one. If he succeeds in doing so, the evaluation of the chance is part of the assessment of the quantum of damage, the range lying somewhere between something that just qualifies as real or substantial on the one hand and near certainty on the other. I do not think that it is helpful to seek to lay down in percentage terms what the lower and upper ends of the bracket should be.

In Allied Maples Group v. Simmons & Simmons (1995), the defendant firm of City solicitors had assisted their client in commercial negotiations for the purchase of a business. But the defendant solicitors negligently failed to try to reinsert a 'warranty' into the prospective agreement. This clause had been initially included in the draft document. But the vendor had removed it from the draft before the deal was concluded. A less advantageous clause had been substituted. The deleted warranty would have protected the buyer. The legal difficulty, however, was to reconstruct the negotiation process and determine whether the vendor would have acceded to this clause being included.

¹⁶⁰ *Ibid.*, at [34].

¹⁶¹ [1987] 3 All ER 748, 755, CA.

¹⁶² [1995] 1 WLR 1602, CA, noted by T. Church, [1996] CLJ 187; considered in *4 Eng Ltd v. Harper* [2008] EWHC 915 (Ch); [2009] Ch 91 (noted by P. Mitchell, (2009) 125 LQR 12–17) (on which see 9.13).

¹⁶³ [1995] 1 WLR 1602, 1614, CA.

The Court of Appeal held that it was appropriate on the facts to award a sum to reflect the 'real' or 'substantial' loss of the chance that the vendor might have made the relevant bargaining concession. Applying that criterion, the majority¹⁶⁴ held that this line had been successfully crossed on the evidence (Millett LJ dissented on this question of assessment, although not on the applicable test).¹⁶⁵

Similarly, in *Jackson v. Royal Bank of Scotland* (2005), the House of Lords upheld a trial judge's award of loss of future business.¹⁶⁶ The claimant imported goods ('doggie-chews') into the UK from the Far East, which he then sold to a UK wholesaler. The defendant bank accidentally revealed to this third party (the wholesaler) details of the 'mark-up' obtained by the claimant importer (the difference between the amount paid when acquiring the merchandise in the foreign market, and the sum charged by the middleman to the third party purchaser). As a result, the claimant's run of deals with this third party was cut short because the wholesaler decided to buy these goods for himself in the Far East. The bank's revelation of that mark-up was a breach of its contractual obligation to maintain the client's confidentiality. The House of Lords held the basic claim for lost future revenue was not too speculative. Nor was the claim too remote, because this type of loss was not outside the parties' contemplation. *But the extent of recoverable future loss was a matter for conjecture.* The claimant could not recover for an indefinite series of prospective deals with a third party over many years. The House of Lords decided that a fair sum was for four lost years of expected revenue (as decided by the trial judge; the Court of Appeal had cautiously reduced this to one year). This award was designed to reflect the sense that transactions between the claimant and the wholesaler might well have petered out in due course even if the defendant bank had not committed this breach of confidentiality.

18.34 Compensation for aggravation or consumer disappointment. The starting point is that, in general, a defendant is not liable for mental distress caused by breach of contract, even though the distress is not too remote a consequence of the breach.¹⁶⁷ The House of Lords' discussion in *Farley v. Skinner* (2002), the leading case, reveals three main exceptions to this proposition:¹⁶⁸

- (1) Proof of 'physical' discomfort (including noise), which engenders such negative feelings.¹⁶⁹

¹⁶⁴ Stuart-Smith and Hobhouse LJ.

¹⁶⁵ Millett LJ, dissenting, would instead have ordered that the matter be re-opened for further evidence.

¹⁶⁶ [2005] UKHL 3; [2005] 1 WLR 377, at [43].

¹⁶⁷ *Addis v. Gramophone Co. Ltd* [1909] AC 488, HL; *Watts v. Morrow* [1991] 1 WLR 1421, 1445, CA, *per* Bingham LJ; *Johnson v. Gore, Wood & Co.* [2002] 2 AC 1, 37–8, HL; *Hamilton Jones v. David and Snape* [2003] EWHC 3147 (Ch); [2004] 1 All ER 657, at [52] ff, Neuberger J; *McGregor on Damages* (18th edn, London, 2009), 3–013 ff.

¹⁶⁸ [2001] UKHL 49; [2002] 2 AC 732, HL, noted D. Capper, (2002) 118 LQR 193 and E. McKendrick and M. Graham, [2002] LMCLQ 161; cf Canada: *Fidler v. Sun Life Assurance Co. of Canada Ltd* [2006] SCC 30; [2006] 2 SCR 3 (Supreme Court of Canada), noted by M. Clapton and M. McInnes, (2007) 123 LQR 26–9; and *Honda Canada Inc. v. Keays* [2008] SCC 39; (2008) 294 DLR (4th) 371 (Supreme Court of Canada), noted by M. McInnes, (2009) 125 LQR 16.

¹⁶⁹ E.g. *Farley v. Skinner* [2001] UKHL 49; [2002] 2 AC 732, HL, and *Hobbs v. London and South Western Railway Co.* (1875) LR 10 QB 111, CA (physical inconvenience of late-night walk in the rain; considered in

- (2) The contract has as one of its main¹⁷⁰ purposes (a) the avoidance of aggravation (such as liability of surveyors commissioned to inspect property or the liability of lawyers retained to obtain injunctive relief against violent or threatening persons); or (b) conferment of pleasure (holiday companies¹⁷¹ or photographers at 'one-off' special occasions).¹⁷²
- (3) The 'consumer surplus' measure of compensation;¹⁷³ the phrase 'consumer surplus' denotes a non-pecuniary type of non-performance; it is vindicated by a contractual 'solatium', or loss of amenity award; such a claim is for 'loss' which, although palpable to consumers, is not reflected concretely in the 'market'. The leading discussion of the 'consumer surplus' concept is the *Ruxley* case (1996)¹⁷⁴ (18.29), where a 'consumer' recovered a modest sum of £2,500 for the disappointment he suffered because the other party had failed to construct a swimming pool of specified depth.

As Lord Scott said in the *Farley* case, the difference between (2) and (3) is that (2) involves consequential loss, whereas (3) involves denying the claimant the benefit of a promised performance.

- 18.35** There is a regime for non-tangible harm in the field of employment disputes.¹⁷⁵ In particular, actions for bullying at work can produce extensive liability, and such claims for breach of duty can straddle contractual and tortious obligations.¹⁷⁶
- 18.36** *Tort claims for loss of business opportunities.* The true difference between contractual and tort damages is not that the former alone can protect expectations, but that contractual

Milner v. Carnival plc (trading as Cunard) [2010] EWCA Civ 389; [2010] 3 All ER 701, at [31] ff; breach of landlord's repairing obligation, *English Churches Housing Group v. Shine* [2004] EWCA Civ 434.

170 *Farley v. Skinner* [2001] UKHL 49; [2002] 2 AC 732, at [24], *per* Lord Steyn: 'a major or important object of the contract is to give pleasure, relaxation or peace of mind.'

171 *Milner v. Carnival plc (trading as Cunard)* [2010] EWCA Civ 389; [2010] 3 All ER 701, at [32] ff, for a review of the holiday cases; a trend of making rather ungenerous awards was noted, without criticism, at [54] ff; and disappointment damages for a most unhappy 'luxury cruise' were pegged at £4,500 for the wife and £4,000 for the husband.

172 *Farley v. Skinner* [2001] UKHL 49; [2002] 2 AC 732, at [52] to [69]; solicitors have been liable under this heading: *Heywood v. Wellers* [1976] QB 446, CA, and *Hamilton Jones v. David & Snape* [2003] EWHC 3147 (Ch); [2004] 1 WLR 921, Neuberger J.

173 *Ruxley Electronics and Construction Ltd v. Forsyth* [1996] AC 344, HL; D. Harris, A. Ogus and J. Phillips, (1979) 95 LQR 581, cited by Lord Mustill in the *Ruxley* case.

174 *Ruxley Electronics and Construction Ltd v. Forsyth* [1996] AC 344, HL; literature on the *Ruxley* case includes H. Beale in P. B. H. Birks (ed.), *Wrongs & Remedies in the Twenty-First Century* (Oxford, 1996), 227–9; J. O'Sullivan, in F. D. Rose (ed.), *Failure of Contract* (Oxford, 1997), chapter 1; E. Peel, in *ibid.*, at chapter 2; B. Coote, [1997] CLJ 537, especially on facts (538–9) and proposals for reform (566, 569–70); J. Cartwright, in A. Burrows and E. Peel (eds.), *Commercial Remedies: Current Issues and Problems* (Oxford, 2003), 9–13.

175 On the interaction of the statutory system of compensation for unfair dismissal and common law duties of 'trust and confidence', see *Johnson v. Unisys Ltd* [2001] UKHL 13; [2003] 1 AC 518; *Dunnachie v. Kingston-upon-Hull City Council* [2004] UKHL 36; [2005] 1 AC 226; *Eastwood v. Magnox Electric plc* [2004] UKHL 35; [2005] 1 AC 503.

176 *Helen Green v. DB Group (UK) Ltd* [2006] EWHC 1898 (QB), Owen J.

undertakings and warranties can be the *source of the relevant protected expectations*. It then becomes necessary for contractual damages to be awarded to vindicate those expectations, which – in the absence of the relevant undertaking or warranty – would not have arisen. Warranted expectations are, therefore, contractually supported hopes *which would not exist if the party had not received a promise or assurance under the relevant contract*. For example, if D warrants that the subject matter of the contract will have a certain quality, but it lacks it, P can obtain contractual damages for the gain which would have accrued if the subject matter had possessed that quality. That type of pure expectation is protected only by a contractual term or collateral warranty. But *when the chance of gain exists independently of a contractual promise made by the party now in breach*, tort damages can reflect the claimant's economic loss. This is the basis of the successful tort claims (both based on deceit) upheld in *East v. Maurer* (1991)¹⁷⁷ and in *Clef Aquitaine SARL v. Laporte Materials (Barrow) Ltd* (2001).¹⁷⁸ In *East v. Maurer* (1991), the claimant bought a hairdressing salon after the defendant had deceitfully tricked her into believing that he would no longer work in his second salon, but the vendor intended all along that he would continue to work at the other salon. In *Clef Aquitaine SARL v. Laporte Materials (Barrow) Ltd* (2001), the claimant took a distributorship to supply the defendant's products in France, but the claimant had been misled during the negotiations by the defendant's lie concerning its 'bottom price' for selling products to wholesalers. Both cases were considered in *4 Eng Ltd v. Harper* (2008).¹⁷⁹ All three cases are examined at 9.13.

18.37 *Comparison of contractual and tort damages (actions for deceit¹⁸⁰ or negligence)*. The following example assumes that Y bought X's car for £5,000 after X had warranted that it had done '50,000 miles only', and the car has in fact done 100,000 miles. The car's actual value in that state is £4,000. If it had done only 50,000 miles, it would have been worth £12,000. Consider the following claims:

- (1) In contract, Y can obtain as damages the difference between the market value of the goods at the time of delivery, £4,000 (not the price paid) and the value the car would have had if the car had complied with its warranty, £12,000;¹⁸¹ and so Y's loss of bargain measure is worth £8,000; that is, the difference between the value of goods received and their warranted value: section 53(3) of the Sale of Goods Act 1979.
- (2) In tort, Y can obtain as damages the difference between the price paid, £5,000, and the product's actual value, £4,000 (the representee's immediate out-of-pocket loss); and so £1,000 would be awarded if Y's claim were successful in tort on the basis of

177 [1991] 1 WLR 461 CA, noted J Marks (1992) 108 LQR 386; *East v. Maurer* approved by Lord Steyn in *Smith New Court* case, [1997] AC 254, HL.

178 J. Cartwright *Misrepresentation, Mistake and Non-Disclosure* (2nd edn, London, 2007), 5–39.

179 [2008] EWHC 915 (Ch); [2008] 3 WLR 892, David Richards J at [42] to [58]; noted by P. Mitchell, (2009) 125 LQR 12–17.

180 *Derry v. Peek* (1889) 14 App Cas 337, HL; *Smith New Court* case, [1997] AC 254, HL.

181 It is the buyer's loss on an immediate notional resale which counts: the 'difference between what he can get for the car and what he might have got for the car'.

- deceit or breach of a common law duty to avoid negligent misstatement. Therefore, Y will seek the contractual measure in (1) rather than the tortious measure in (2).
- (3) Where the warranted value is less than the agreed price for the product ('bad bargain'), Y's contractual entitlement will be zero (no 'loss of expectation') (although nominal damages will be available to reflect the technical nature of the breach). Instead, only tortious (non-nominal) damages will assist the claimant: tort law will give Y the difference between the sum paid and the (lower) value of the car delivered – the claimant's out-of-pocket harm. If the car would have been worth only £4,000 even if it had only done 50,000 miles, that is, even if the warranty had been accurate, but Y had paid more than that true value (here, £5,000, an excess of £1,000), Y will have made a 'bad bargain'; Y's contractual damages claim will result in nominal damages. But, on these same facts, Y can still recover £1,000 in the torts of deceit or negligence, the difference between the sum paid and the value of the car delivered; that is the amount which Y has wasted as a result of X's fraud or misrepresentation. These torts are wrongs committed independently of the seller's breach of contract.

Limits on damages claims

- 18.38** The limits which will be examined are: (1) causation; (2) remoteness and the satellite concept of 'scope of duty'; (3) mitigation of loss; and (4) contributory negligence. (1) to (3) apply to all contractual damages claims. But (4) is confined to breach of contractual duties of care where the obligation overlaps with a tortious duty of care.
- 18.39** *Causation*. The loss must have been caused by the defendant's breach. In contract law, the notion of causation imposes not just the 'but for' requirement, whether the loss would not have occurred without the breach, but the more technical requirement that the breach was a *legally significant cause* of the alleged loss. Two cases will be cited to illustrate this: *Galoo v. Bright Grahame Murray* (1994)¹⁸² and *Supershield Ltd v. Siemens Building Technologies FE Ltd* (2010).¹⁸³

In *Galoo v. Bright Grahame Murray* (1994),¹⁸⁴ the defendant accountancy firm breached its contract by negligently failing to carry out an audit of two companies. Those companies later became insolvent, whereupon their shareholders and liquidators sought compensation against the defendants. The claim foundered on the question of causation. The Court of Appeal held that the defendant's breach had not been a sufficient factor in the companies' subsequent commercial activity. Instead, the court discerned an independent set of decisions by the companies' directors to continue to trade.

¹⁸² [1994] 1 WLR 1360, CA.

¹⁸³ [2010] EWCA Civ 7; [2010] NPC 5.

¹⁸⁴ [1994] 1 WLR 1360, CA; A. S. Burrows, *Remedies for Torts and Breach of Contract* (3rd edn, Oxford, 2004), 107.

In *Supershield Ltd v. Siemens Building Technologies FE Ltd* (2010),¹⁸⁵ the owners ('Deka') and occupiers (Slaughter and May) of One Bunhill Row, a law office in the City of London, suffered loss when the basement of a new building flooded. The ultimate cause of the flood was a sub-contractor's failure to tighten sufficiently a nut on the water valve, which controlled the level of water within the building's sprinkler tanks. The owner/occupiers' claim against the sprinkler contractor (Siemens) was settled in 2008, following mediation, for roughly 50 per cent of the claim [in fact, there were two other lead claimants, beneficiaries of that settlement, but this does not matter for our purposes]. Siemens now sought damages for the amount of that settlement against Supershield, the contractor to which Siemens had delegated the task of installing both the sprinkler tank and its valve. The Siemens/Supershield dispute was based on breach of contract by Supershield.

Supershield attempted to defend itself by suggesting that, ordinarily, given the elaborate 'back-up measures' employed within this basement, the 'loose nut' should not have caused this calamity; and so Supershield attempted to pass responsibility by alleging failure of others to maintain adequate back-up systems: blockages in the drains of the overflow tank, lack of (human) monitoring of a warning system activated by the overflow, and failure to spot the loose nut during routine maintenance.

But Supershield's defence failed. The Court of Appeal upheld Ramsey J's decision that the settlement made by Siemens had been reasonable. In particular, the Court of Appeal agreed that Ramsey J had been right to reject Supershield's two defences: (1) that the settlement loss was not caused by Supershield and (2) that this loss was too remote. On the question of causation, Toulson LJ said:¹⁸⁶

Ramsey J considered that the overflowing of water from the sprinkler tank which resulted from the failure of the connection between the ball valve and lever arm was an effective cause of the flood. The blockage of the drains did not take away the potency of the overflow to cause damage, but rather failed to reduce it. I see no error in that approach. On the contrary, it would have been a rash lawyer who would have advised Siemens that it was likely to succeed on the causation issue, let alone that it could be confident of doing so.

And on (2), the question of remoteness (18.40 ff), the Court of Appeal held that Supershield could not, under limb 2 of *Hadley v. Baxendale* (1854) (18.43 case (1)), avoid responsibility by suggesting that Siemens and Supershield understood that other 'precautions adopted for the basement' exonerated Supershield from liability for the very slight risk of catastrophic harm resulting from failure to tighten the ball valve nut.¹⁸⁷ The Siemens case is further discussed at 18.39 and 18.43, on the 'remoteness point'.

¹⁸⁵ [2010] EWCA Civ 7; [2010] NPC 5.

¹⁸⁶ *Ibid.*, at [32] and [33].

¹⁸⁷ *Supershield Ltd v. Siemens Building Technologies FE Ltd* [2009] EWHC 927 (TCC), at [106] to [112], *per* Ramsey J.

18.40 *Remoteness*.¹⁸⁸ The leading cases are set out at 18.43. A contractual claim for compensation will fail if the relevant loss is too ‘remote’, having regard to the parties’ field of ‘contemplation’ at the time the contract was formed. The contractual ‘remoteness of damage’ doctrine can be formulated as follows:

The defendant in breach of contract is only liable for substantial damages (as distinct from the award of nominal or token damages) if the relevant loss was reasonably contemplated by both parties at the time of the contract’s formation as a serious possibility, taking into account (a) (‘limb 1’) the ordinary course of things and (b) (‘limb 2’) any special knowledge which the defendant had at that point. As for (b), the special information must be brought home to the defendant in circumstances indicating that contractual responsibility for that risk is now borne by him.¹⁸⁹ For most claims, it is enough that the contemplation relates to the type of loss;¹⁹⁰ but in the case of claims for loss of profits, the contemplation must extend to the scale of profits.

Four introductory remarks will be made. First, the expression ‘serious possibility’ enjoys House of Lords’ support,¹⁹¹ and is preferred by Burrows.¹⁹² The law has attempted to distinguish (a) degrees of likelihood which are reasonably contemplated in the ordinary course of things, without requiring these to be quite likely to occur, from (b) chances which are simply out of the ordinary, because they are likely to occur only in a ‘small minority of cases’. In *Supershield Ltd v. Siemens Building Technologies FE Ltd* (2010),¹⁹³ Toulson LJ cited the following passage from Lord Reid’s speech in *‘The Heron II’* (1969):¹⁹⁴

A type of damage which was plainly foreseeable as a real possibility but which would only occur in a small minority of cases cannot be regarded as arising in the usual

188 See 18.43 for analysis of the line of cases stemming from *Hadley v. Baxendale* (1854) 9 Exch 341; on its history, see R. Danzig, (1975) 4 *Journal of Legal Studies* 249; F. Faust, (1994) 15 *Journal of Legal History* 41; D. J. Ibbetson, *A Historical Introduction to the Law of Obligations* (Oxford, 1999), 229–31; M. Lobban, in W. Cornish, J. S. Anderson, R. Cocks, M. Lobban, P. Polden and K. Smith, *The Oxford History of the Laws of England*, vol. XII, 1820–1914: *Private Law* (Oxford, 2010), 541 ff; A. W. B. Simpson, (1975) 91 LQR 247, 273–7; W. Swain, ‘The Classical Model of Contract: The Product of a Revolution in Legal Thought’ (2010) 30 LS 513, 531; and G. T. Washington, (1932) 48 LQR 90, 97 ff; on its modern application, see A. S. Burrows, *Remedies for Torts and Breach of Contract* (3rd edn, Oxford, 2004), 83 ff; *McGregor on Damages* (18th edn, London, 2009), 6–155 ff; A. Tettenborn (with D. Wilby and D. Bennett), *The Law of Damages* (London, 2003), chapter 6, at 127 ff; A. Kramer, in N. Cohen and E. McKendrick (eds.), *Comparative Remedies for Breach of Contract* (Oxford, 2005), 249; A. M. Tettenborn, (2007) 23 *Journal of Contract Law* 120; A. Robertson, (2008) 28 LS 172; J. Gordley, ‘The Foreseeability Limitation on Liability in Contract’, in A. Hartkamp and C. Joutstra (eds.), *Towards a European Civil Code* (3rd edn, Nijmegen, 2004), chapter 11. On the *Transfield* case, [2008] UKHL 48; [2009] 1 AC 61 (18.43 case (5) below), see Lord Hoffmann, (2010) 14 *Edinburgh Law Review* 47–61; D. Foxton, [2009] LMCLQ 461–87; D. McLaughlan, (2009) 9 *Oxford University Commonwealth Law Journal* 109–39; J. O’Sullivan, [2009] CLJ 34–7; G. Gordon, (2009) 13 *Edinburgh Law Review* 125–30; E. Peel, (2009) 125 LQR 6–12; A. Kramer, (2009) 125 LQR 408–15; P. C. K. Wee, [2010] LMCLQ 150–76.

189 *Mulvenna v. Royal Bank of Scotland plc* [2003] EWCA Civ 1112, at [24] and [25], *per* Waller LJ.

190 *Parsons v. Uttley Ingham* [1978] QB 791, CA; *Brown v. KMR Services Ltd* [1995] 4 All ER 598, CA.

191 Lord Walker in the *Transfield* case, [2008] UKHL 48; [2009] 1 AC 61, at [76], noting *‘The Heron II’* [1969] 1 AC 350, 400, 415, 425, HL, *per* Lords Morris, Pearce and Upjohn, who ‘approved the expressions “real danger” and “serious possibility”’, although Lord Reid in *‘The Heron II’* at 390 disapproved the latter formulation.

192 A. S. Burrows, *Remedies for Torts and Breach of Contract* (3rd edn, Oxford, 2004), 88, 94.

193 [2010] EWCA Civ 7; [2010] NPC 5, at [37].

194 [1969] 1 AC 350, 385, HL.

course of things or be supposed to have been in the contemplation of the parties: the parties are not supposed to contemplate as grounds for the recovery of damage any type of loss or damage which on the knowledge available to the defendant would appear to him as only likely to occur in a small minority of cases.

The second introductory comment is that ‘limbs 1 and 2’ of the *Hadley v. Baxendale* (1854) test (see above) are now regarded as parts of a composite rule or even a ‘principle’. Lord Mance commented in *Sempra Metals Ltd v. Inland Revenue Commissioners* (2007):¹⁹⁵ ‘The two limbs of *Hadley v. Baxendale* 9 Exch 341 are the practical expression of a single principle (inspired by the civil law) that parties should only be liable for damages which were, when they contracted, within their contemplation in the event of a breach.’ And Lord Walker in *Jackson v. Royal Bank of Scotland plc* (2005)¹⁹⁶ said: ‘[T]he common ground of the two limbs is what the contract-breaker knew [limb 2] or must be taken to have known [limb 1], so as to bring the loss within the reasonable contemplation of the parties.’ And Lord Walker observed that Lord Reid had made this point in ‘*The Heron II*’ (1969).¹⁹⁷

The third introductory comment is this: the main context where the English contractual remoteness test has precluded recovery of damages for breach of contract concerns *unusual loss consequent on delayed or interrupted supply of goods or services*.

There are four leading reported cases on that problem, each of them decided in favour of the guilty party:

- (1) In *Hadley v. Baxendale* (1854)¹⁹⁸ (18.43 case (1)), the defendant carrier was not liable for the customer’s production losses attributable to delayed delivery of equipment if that loss was a special vulnerability not brought home to the carrier at the time of the contract’s formation.
- (2) In the *Victoria Laundry* case (1949)¹⁹⁹ (18.43 case (2)), the defendant supplier of an industrial boiler was not liable to pay compensation for loss of profits arising from an ‘exceptionally lucrative’ deal between the claimant and a third party; the defendant would be liable only for ‘ordinary’ levels of lost profits.
- (3) In *Balfour Beatty Construction Ltd v. Scottish Power* (1994)²⁰⁰ (18.44 at (1)), the defendant supplier of electricity was not liable for losses caused by an interruption in the flow of electricity to a building site, where cement was being used to construct pillars supporting a roadway. As a result of the power shutdown, the pursuer had had to redo some of the construction work, at considerable expense.

195 [2007] UKHL 34; [2008] 1 AC 561, at [215]; on this case, see 18.64.

196 [2005] 1 WLR 377, HL, at [46] to [48].

197 [1969] 1 AC 350, 383–5, HL.

198 (1854) 9 Exch 341.

199 [1949] 2 KB 528, CA.

200 1994 SLT 807; *The Times*, 23 March 1994 (a Scots case taken on final appeal to the House of Lords); H. MacQueen, [1996] *Juridical Review* 295; A. Burrows, *Understanding the Law of Obligations* (Oxford, 1998), 160 ff.

- (4) In *Transfield Shipping Inc. v. Mercator ('The Achilles')* (2008)²⁰¹ (18.43 case (5)), the defendant charterer was not liable for loss of an attractive rate of hire arranged by the ship-owner in a 'follow-on' charterparty with a third party; the defendant's delay in returning the vessel had forced the owner to agree to accept a lower rate of hire from the third party.

The final introductory remark concerns 'limb 2' of the *Hadley v. Baxendale* test (see the beginning of this paragraph). This was considered in *Supershield Ltd v. Siemens Building Technologies FE Ltd* (2010)²⁰² (see, first, 18.39 for the full facts and a discussion of the question of causation; and, secondly, 18.43 below on the question of remoteness and its connection with the scope of duty test). A sub-contractor had failed, in breach of contract, to tighten a nut on a water valve, but then contended that the consequent flooding of the building was not in reasonable contemplation because both parties had *special knowledge* that back-up systems would normally operate to prevent any real risk of a deluge. The Court of Appeal rejected this defence: otherwise, limb 2 would become a shield for negligent contractors whenever safety systems are known by both parties to be designed (normally) to reduce or eliminate a risk of serious malfunction. Toulson LJ said:²⁰³ '[T]he reason for having a number of precautionary measures is for them to serve as a mutual back up, and it would be a perverse result if the greater the number of precautionary measures, the less the legal remedy available to the victim in the case of multiple failures.'

18.41 *Comparison with non-English 'codes' and the Vienna International Sales Convention.* On this, see 21.02.

18.42 The (relatively pro-defendant) contractual principle of remoteness is to be contrasted with the test applicable to negligence claims in tort, the so-called 'reasonable foreseeability' test in *'The Wagon Mound'* case (1961).²⁰⁴ There are four points of contrast.

- (1) The tort test is now regarded as *more generous to claimants* than the contractual test. The criterion of 'reasonable foreseeability' in the tort of negligence must be distinguished from the more exacting threshold of contemplation demanded in contract. Furthermore, the *Wagon Mound* test in the tort of negligence allows recovery if the *head of loss was reasonably foreseeable*, even if the extent of the loss was not foreseeable. Whereas, in the case of contractual claims for *lost profits*, a distinction

²⁰¹ [2008] UKHL 48; [2009] 1 AC 61.

²⁰² [2010] EWCA Civ 7; [2010] NPC 5.

²⁰³ *Ibid.*, at [44].

²⁰⁴ For the tort test, see *'The Wagon Mound'* [1961] AC 388, PC (summarised by Lord Rodger in *Simmons v. British Steel plc* [2004] UKHL 20; [2004] ICR 585, at [67]); on aspects of the remoteness tests in contract and tort, see A. Kramer, in D. Saidov and R. Cunnington (eds.), *Contract Damages: Domestic and International Perspectives* (Oxford, 2008), chapter 12.

has been made, and remains important, between ordinary loss of profits and loss of exceptional profits, that is, between degrees of loss under the same broad head of lost profits. Thus, in contract law, 'exceptional profits' are not recoverable unless the claimant's special vulnerability has been notified to the defendant (for this possibility in the case of contractual claims, see limb 2 of the test stated in the second paragraph of 18.40 above).

- (2) There is also a difference in the *date for assessment*. The tort test is not restricted to contemplated events assessed at the time of the contract, and indeed, in many tort cases, there will be no contract, merely an accident between strangers. Instead, the tort test operates with respect to facts and circumstances subsisting at the time of the defendant's breach of his duty of care.
- (3) Unlike the position in contract, the tort test is *not subject to a second tier of contemplated facts*, these being special facts notified before the contract was formed. In short, the 'second limb' of the contract test (limb 2 of the test stated in the second paragraph of 18.40 above) does not appear as part of the tort test.
- (4) Finally, Burrows contends that the Court of Appeal's decision in *Brown v. KMR Services Ltd* (1995) (18.44, case (3))²⁰⁵ might be interpreted as deciding that the contract test should apply to both a contractual and a tortious claim when there is a business relationship between the parties giving rise to overlapping obligations in contract and tort.²⁰⁶

18.43 *Leading decisions on the basic test of contractual remoteness.* Five major decisions must be noted (in chronological sequence): *Hadley v. Baxendale* (1854); the *Victoria Laundry* case (1949); '*The Heron II*' (1969); *Parsons v. Uttley Ingham* (1978); and the *Transfield* case (2008).

- (1) *Hadley v. Baxendale* (1854),²⁰⁷ the seminal case on contractual 'remoteness', establishes a twofold test: the loss is not too remote provided it was contemplated by the parties, at the time of the contract's formation, as either (a) loss arising in the ordinary course of things or (b) as loss arising as a natural consequence, taking into account special circumstances communicated to or known by the defendants. Baron Alderson formulated the test as follows:

[Contractual damages] should be such as may fairly and reasonably be considered, either arising naturally, i.e. according to the usual course of things from such breach of contract itself, or such as may reasonably be supposed to have been in the contemplation of both parties, at the time they made the contract as the probable result of the breach of it.²⁰⁸

205 [1995] 4 All ER 598, CA.

206 A. S. Burrows, *Remedies for Torts and Breach of Contract* (3rd edn, Oxford, 2004), 93–4; cf Sir Thomas Bingham MR in the *Banque Bruxelles Lambert* case, [1995] QB 375, 405E, CA (a terse elision of tort and contract tests but without citation of authorities).

207 (1854) 9 Exch 341, Court of Exchequer, Parke, Martin and Alderson BB.

208 *Ibid.*, at 354.

He added:

[The plaintiff's] loss would neither have flowed naturally from the breach of this contract in the great multitude of such cases occurring under ordinary circumstances, nor were the special circumstances, which, perhaps, would have made it a reasonable and natural consequence of such breach, communicated to or known by the defendants.

In *Hadley v. Baxendale* (1854), the defendant carrier (the defendant was the managing director of Pickfords, the leading inland carrier of the age) was hired to carry a broken crankshaft from the claimant's mill at Gloucester to a third party engineer at Greenwich. The claimant did not tell him that this was the only crankshaft and that it was being transported as a pattern to build a replacement. The carrier breached his contract by delivering this item several days late to Greenwich. The plaintiff miller lost five days of operation as a result, for which he claimed lost profits.

Vital to the decision (and contrary to the headnote in the law report) was the fact that the carrier had not been told by the miller, and so did not know, that it was crucial to his business that the crankshaft should be delivered speedily.²⁰⁹ Alderson B said that the ordinary assumption would be that the claimant had a replacement crankshaft, or that there were other reasons why the mill was not capable of being used at this time.

(2) *Victoria Laundry (Windsor) Ltd v. Newman Industries Ltd* (1949)²¹⁰ remains binding Court of Appeal authority that an exceptionally high level of profit will not be recoverable as damages for breach of contract unless the defendant was aware, usually following notice given by the claimant, of this special financial vulnerability.

Asquith LJ gave the court's judgment. He enunciated a set of lucid propositions concerning the contractual remoteness test.²¹¹ However, one of these propositions was rejected by the House of Lords in *'The Heron II'* (1969) (discussed next). The rejected comment was Asquith LJ's suggestion that it is enough that the relevant loss could be foreseen by the parties as 'on the cards' or 'likely'.²¹² As we shall see, the level of likelihood must be higher than that: a test of 'serious possibility' of loss has been adopted.

The defendant vendor agreed to supply an industrial boiler to the defendant. This was a major purchase. It must have been obvious that the claimant would not have a spare boiler, and indeed the defendant knew that the boiler was required for immediate use in the claimant's business. In breach of contract, the defendant supplied the item five months late. The claimant was held to be entitled to recover ordinary profits on contracts with customers.

209 As clarified by Asquith LJ in the *Victoria Laundry* case, [1949] 2 KB 528, 537, CA.

210 [1949] 2 KB 528, CA.

211 *Ibid.*, at 539–40, propositions (1) to (6).

212 *Ibid.*, at 540.

The late supply of the main boiler in the *Victoria Laundry* case can be contrasted with the situation in *Hadley v. Baxendale*, where it was reasonable to expect a miller to have had a replacement crankshaft.²¹³ However, the Court of Appeal in the *Victoria Laundry* case held that the defendant's liability did not extend to exceptionally lucrative profits to be obtained under a deal with the government, the Ministry of Supply, because the latter were not foreseeable in the ordinary course of things and the defendant had received no notification of the claimant's intention to expand his business in this fashion.²¹⁴

In the *Transfield* case (2008) (on which see case (5) below), Lord Hoffmann commented with approval on the *Victoria Laundry* decision:²¹⁵

[T]he Court of Appeal [in the *Victoria Laundry* case] did not regard 'loss of profits from the laundry business' as a single type of loss. They distinguished losses from 'particularly lucrative dyeing contracts' as a different type of loss ... The vendor of the boilers would have regarded the profits on these contracts as a different and higher form of risk than the general risk of loss of profits by the laundry.

(3) The House of Lords in *C Czarnikow Ltd v. Koufos ('The Heron II')* (1969)²¹⁶ emphasised that the test of remoteness in contract requires contemplation, actual or presumed, of the relevant loss as a 'serious possibility' (although the speeches could not pinpoint a single, agreed formulation, something which attracted criticism).²¹⁷ The House of Lords rejected the test of a mere likelihood or an 'on the cards' possibility.²¹⁸

'The Heron II' concerned a charterparty. The ship deviated en route to Basra (in Iraq) where the defendant was to unload the claimant's consignment of sugar. The defendant did not know that the claimant intended to sell the sugar in Basra. But the defendant did know that there was a market for this commodity at the port of destination. The sugar was delivered nine days late. During this period, its price had fallen. The House of Lords upheld the arbitrator's award of damages for this difference in value.²¹⁹

Lord Reid required a 'very substantial degree of probability' or an event which is 'not unlikely';²²⁰ Lord Morris was content with 'liable to result or at least not unlikely to result';²²¹ Lord Hodson went for 'liable to result'²²² (although this was rejected by Lord Reid);²²³ Lord

213 *Ibid.*, at 541, 544.

214 *Ibid.*, at 543.

215 [2008] UKHL 48; [2009] 1 AC 61, at [22], *per* Lord Hoffmann.

216 [1969] 1 AC 350, HL.

217 See the harsh comments made in the USA (cited in A. Burrows and E. Peel (eds.), *Commercial Remedies: Current Issues and Problems* (Oxford, 2003), 33); and A. Ogus, *The Law of Damages* (London, 1973), 76, said: '[T]he hapless student is confronted by yet more verbiage.'

218 [1969] 1 AC 350, 424–5, *per* Lord Upjohn.

219 Rejecting the contrary decision in *'The Parana'* (1877) 2 PD 118, CA.

220 *Ibid.*, at 388.

221 *Ibid.*, at 406.

222 *Ibid.*, at 410–11.

223 *Ibid.*, at 410–11.

Pearce referred to a 'serious possibility' or 'real danger', equating these with 'liable to result';²²⁴ and Lord Upjohn agreed with the 'real danger' or 'serious possibility' formulations.²²⁵

This case has now been authoritatively summarised by Toulson LJ in *Supershield Ltd v. Siemens Building Technologies FE Ltd* (2010),²²⁶ who cited the following passage from Lord Reid's speech in *'The Heron II'* (1969):²²⁷

[A] type of damage which was plainly foreseeable as a real possibility but which would only occur in a small minority of cases cannot be regarded as arising in the usual course of things or be supposed to have been in the contemplation of the parties: the parties are not supposed to contemplate as grounds for the recovery of damage any type of loss or damage which on the knowledge available to the defendant would appear to him as only likely to occur in a small minority of cases.

Similarly, in the *Transfield* case (2008) (on which see case (5) below), Lord Rodger neatly summarised the doctrine purified by *'The Heron II'* as follows:²²⁸

[I]n the absence of special knowledge, a party entering into a contract can only be supposed to contemplate the losses which are likely to result from the breach in question – in other words, those losses which will generally happen in the ordinary course of things if the breach occurs.

And Lord Hoffmann, writing in the *Edinburgh Law Review*, commented on *'The Heron II'* as follows:²²⁹

Lord Reid's test in *'The Heron II'* [is] whether the type of loss was 'not unlikely', a 'serious possibility'. *'The Heron II'* contains a thesaurus of expressions which can be used to describe the necessary degree of probability, but no one has said that Lord Reid's test was wrong. It is in practice the one most frequently adopted.

(4) *H Parsons (Livestock) Ltd v. Uttley Ingham & Co. Ltd* (1978)²³⁰ contains a majority view (adopted by Scarman and Orr LJ) that it is enough in the case of *damage to property* (as on the facts of this case) or perhaps *personal injury* that the parties contemplated, in accordance with the contractual remoteness test, that the relevant *head of loss would be liable to result from breach: there is no need to contemplate more precisely the degree or extent of loss*. (The *Victoria Laundry* case (1949) (on which see case (2) above), however, requires a distinction to be drawn between ordinary and exceptional levels of *commercial profit*. This case remains good law in that context.)

224 *Ibid.*, at 415.

225 *Ibid.*, at 425.

226 [2010] EWCA Civ 7; [2010] NPC 5, at [37].

227 [1969] 1 AC 350, 385, HL.

228 [2008] UKHL 48; [2009] 1 AC 61, at [52], *per* Lord Rodger.

229 (2010) 14 *Edinburgh Law Review* 47, 51.

230 [1978] QB 791, CA.

In the *Parsons* case, the defendant supplied and installed at the claimant's pig farm a hopper for the storage of pig nuts. But the defendant failed to adjust the top of the hopper so that it would provide ventilation to its contents, and so the nuts became mouldy. The claimant fed them to his pigs, who fell very ill, 254 fatally, with intestinal poisoning (*E coli*) (the question of the claimant's contribution to this was not fully addressed in the main report of this decision, although the issue was raised at trial, according to another report).²³¹

The Court of Appeal unanimously held that the property loss sustained on these facts was not too remote. Lord Denning MR explained this as a type of loss (physical damage to property) other than loss of profits and said that the tort test established in the *Wagon Mound* (1961) line of cases should apply, namely, reasonable foreseeability.²³² In his view, the more demanding *Hadley v. Baxendale* (1854) remoteness test should be confined to contractual claims for loss of profits.²³³ But this is not the law. He said:²³⁴ '[T]he three leading cases of *Hadley v. Baxendale* (1954), *Victoria Laundry (Windsor) Ltd v. Newman Industries Ltd* (1949) and *The Heron II* (1969) ... were all "loss of profit" cases: and the test of "reasonable contemplation" and "serious possibility" should, I suggest, be kept to that type of loss or, at any rate, to economic loss.'

But in the *Parsons* case (1978), Scarman and Orr LJ rejected Lord Denning's revision of the law as heterodox. They held that the farmer's loss should be characterised as 'illness' suffered by his livestock. The parties should be taken to have contemplated this as 'a serious possibility'.²³⁵ There was no need for the parties to have foreseen the fatal nature of that illness.²³⁶

(5) The leading case is now *Transfield Shipping Inc. v. Mercator ('The Achilleas')* (2008).²³⁷ A summary follows. The points in the summary are expanded in the text below.

A charterer was nine days late in returning a vessel to the owner. Expecting that the vessel would be back on time, the owner had already arranged a new charter for several months at an attractive rate with Z. Because the vessel was redelivered late, the owner was forced to lower that attractive rate, especially because the market rate had recently fallen (the reduction was US\$8,000 a day and the new charter with Z was to last for many months).

231 [1978] QB 791, 810A (R. Cooke, [1978] CLJ 288, 296, notes the Lloyd's Report on this aspect: [1977] 2 Lloyd's Rep 522, 25, CA); cf *Lambert v. Lewis* [1982] AC 225, 276–7, HL (accident resulting in injury to A, as a result of Z continuing to drive with an obviously defective coupling connecting a trailer to his car).

232 [1978] QB 791, 801–4, CA, citing '*The Wagon Mound*' (No. 1) [1961] AC 388, PC, and '*The Wagon Mound*' (No. 2) [1967] 1 AC 617, PC.

233 Adopting H. L. A. Hart and A. Honoré, *Causation in the Law* (Oxford, 1959), 281–7; now (2nd edn, Oxford, 1985), 320–1.

234 [1978] QB 791, 802–3, CA.

235 *Ibid.*, at 805–6.

236 *Ibid.*, at 813.

237 [2008] UKHL 48; [2009] 1 AC 61: Lord Hoffmann, (2010) 14 *Edinburgh Law Review* 47–61; D. Foxton, [2009] LMCLQ 461–87; D. McLaughlan, (2009) 9 *Oxford University Commonwealth Law Journal* 109–39; J. O'Sullivan, [2009] CLJ 34–7; G. Gordon, (2009) 13 *Edinburgh Law Review* 125–30; E. Peel, (2009) 125 LQR 6–12; A. Kramer, (2009) 125 LQR 408–15; P. C. K. Wee, [2010] LMCLQ 150–76.

The owner failed to recover this exceptionally severe loss and was restricted to the ordinary measure, the difference between the hire rate applicable between claimant and defendant for the number of days' delay (nine days) and the market hire rate prevailing during those nine days. The decision contains two strands: reasoning by reference to remoteness and scope of duty. Lords Rodger and Walker and Baroness Hale justified this result by reference to ordinary remoteness principles. One might explain that result as consistent with the *Victoria Laundry* case (1949):²³⁸ denial of liability for a specially lucrative dependent contract, the defendant not having been informed of this special risk at the time of formation. But, in the *Transfield* case, Lord Hoffmann preferred to base this result on the notion of 'scope of duty'. Baroness Hale expressed concern that the scope of duty approach might introduce uncertainty into disputes concerning commercial damages claims. Lord Walker suggested that the contractual remoteness test is already sufficiently sensitive to the parties' implicit allocation of risk and, therefore, there is no need to invoke the 'scope of duty' concept.

The Transfield case in detail

Facts

M chartered its ship to T, the vessel to be returned on 2 May 2004.²³⁹ After M was reassured by T that the ship would be back by that date, M agreed a succeeding charter with a third party, Z, for a period of about four to six months, starting 8 May 2004, at a rate of US\$39,500 per day. In breach of contract, T did not return the ship to M until 11 May 2004, nine days late. As a result of this delay, M had no commercial option other than to renegotiate its hire terms with Z. M agreed to reduce the rate by US\$8,000 per day. M did so because the market had fallen sharply. Z would only take the vessel at a reduced price.

Decision

A majority of a panel of three arbitrators awarded damages at US\$8,000 per day. This award was upheld on first appeal by Christopher Clarke J and on second appeal by the Court of Appeal. The House of Lords held that this award was excessive. Instead, the House held that the claimant was entitled only to the difference – for the nine days of hire (the amount of the delay) – between the lower charter rate and the then prevailing market rate. The reasoning in the case is, however, schizophrenic, one group of judges preferring to adopt traditional 'remoteness' reasoning, but Lord Hoffmann invoking (his own favoured) scope of duty test (on that test, see his leading speech in the *Banque Bruxelles/SAAMCO* case (18.45)).

Remoteness

Lord Rodger (Lord Walker and Baroness Hale agreeing) decided the *Transfield* case according to the first limb of the *Hadley v. Baxendale* test. He regarded the claimant's inability to maintain its advantageous 'follow-on' charterparty as a loss outside the ordinary course of things:²⁴⁰

238 [1949] 2 KB 528, CA.

239 [2008] UKHL 48; [2009] 1 AC 61.

240 *Ibid.*, at [60], *per* Lord Rodger (with Lord Walker's and Baroness Hale's concurrence).

[At the relevant date of contracting] neither party would reasonably have contemplated that an overrun of nine days would 'in the ordinary course of things' cause the owners the kind of loss for which they claim damages ... *It occurred in this case only because of the extremely volatile market conditions which produced both the owners' initial (particularly lucrative) transaction, with a third party, and the subsequent pressure on the owners to accept a lower rate for that fixture.* [At the relevant date of contracting], this loss could not have been reasonably foreseen as being likely to arise out of the delay in question.

In the emphasised sentence, Lord Rodger is making the point that the market rate for hiring ships had fluctuated in an extreme way during the currency of the relevant contract: the claimant had at first been able to demand a high level of hire in the 'follow-on' contract; but then the claimant had been induced by Z, the third party, to reduce that price to reflect the subsequent market fall. This seesaw effect was quite out of the ordinary, in Lord Rodger's opinion.

Scope of duty test

Lord Hoffmann (who had 'invented' the scope of duty test in the *Banque Bruxelles/SAAMCO* case (on which see 18.45)) said in the *Transfield* case:²⁴¹

If ... one considers what these parties, contracting against the background of market expectations found by the arbitrators, would reasonably have considered the extent of the liability they were undertaking, I think it is clear that they would have considered losses arising from the loss of the following fixture [that is, the owner's re-chartering of the vessel to the third party] a type or kind of loss for which the charterer was not assuming responsibility.

Scepticism towards the scope of duty test

In the *Transfield* case, Baroness Hale strongly favoured the 'remoteness' test rather than the 'scope of duty' concept preferred by Lord Hoffmann. She said:²⁴²

I am not immediately attracted to the idea of introducing into the law of contract the concept of the scope of duty which has perforce had to be developed in the [tort] of negligence. The rule in *Hadley v. Baxendale* asks what the parties must be taken to have had in their contemplation, rather than what they actually had in their contemplation, but the criterion by which this is judged is a factual one.

Baroness Hale continued:

Questions of assumption of risk depend upon a wider range of factors and value judgements. This type of reasoning ... could easily be at the expense of justice in some

²⁴¹ *Ibid.*, at [23], *per* Lord Hoffmann: Lord Hope supported this approach, and Lord Walker at [87] approved it, even though his own reasons were based on the 'remoteness analysis'.

²⁴² *Ibid.*, at [93], *per* Baroness Hale.

future case. It could also introduce much room for argument in other contractual contexts. Therefore ... I would prefer ... the narrower [remoteness] ground identified by Lord Rodger.

Integration of the remoteness and scope of duty tests in claims concerning breach of contract

The preceding discussion reminds us that the contractual remoteness test is not just a question of abstract predictability but an objective assessment of *common expectations concerning the risk of various forms of breach*. If this is correct, the principle of ‘Occam’s Razor’ (avoidance of conceptual duplication) requires that the scope of duty test should not be used in tandem with the *contractual test of remoteness*. Instead, the scope of duty test should be used only to supplement *the different test in tort* (based upon liability for all consequences, provided only they are reasonably foreseeable: see 18.42 on the *Wagon Mound* test). In the *Transfield* case (2008), Lord Walker said:²⁴³

The diversity of opinion in *The Heron II* (1969) has another and more important significance. Other passages in the speeches show that their Lordships had well in mind (but did not, perhaps, spell out at length) that it is not simply a question of probability. It is also a question of what the contracting parties must be taken to have had in mind, having regard to the nature and object of their business transaction. If a manufacturer of lightning conductors sells a defective conductor and the customer’s house burns down as a result, the manufacturer will not escape liability by proving that only one in a hundred of his customers’ buildings had actually been struck by lightning ... The need for the loss suffered to be within the horizon of the parties’ contemplation ... makes it less important to define its degree of probability with any precision. Arguably a vague expression (such as ‘real possibility’) is actually preferable, because it is more flexible, once it is understood that what is most important is the common expectation, objectively assessed, on the basis of which the parties are entering into their contract.

Consistent with this, one commercial judge has dismissed the suggestion that the scope of duty test now subsists in parallel to the remoteness test. Thus, Flaux J in *ASM Shipping Ltd of India v. TTMI Ltd of England* (*‘The Amer Energy’*) (2008) said:²⁴⁴

I do not consider that the House of Lords [in the *Transfield* case] (at least the majority of their Lordships) were intending to lay down some completely new test as to recoverability of damages in contract and remoteness different from the so-called rule in *Hadley v. Baxendale* ... To the extent that Lord Hoffmann was purporting to lay down some new test as to recoverability of damages in contract, he was in a minority.

And, in *Supershield Ltd v. Siemens Building Technologies FE Ltd* (2010), Toulson LJ, attempting to integrate the scope of duty test into the matrix of factors underpinning

243 *Ibid.*, at [78], *per* Lord Walker, noting support for this approach in the literature: A. Kramer, in N. Cohen and E. McKendrick (eds.), *Comparative Remedies for Breach of Contract* (Oxford, 2005), 249; A. M. Tettenborn, (2007) 23 *Journal of Contract Law* 120; A. Robertson, (2008) 28 LS 172.

244 [2009] 1 Lloyd’s Rep 293, at [17] to [19].

the *Hadley v. Baxendale* test, said:²⁴⁵ '[T]he question of remoteness cannot be isolated from consideration of the purpose of the contract and the scope of the contractual obligation.' Adopting this helpful suggestion, which echoes Lord Walker's comments in the *Transfield* case, the true question, it is submitted, is whether the defendant's obligation exposes him to liability for the loss which has in fact occurred. The remoteness question is not confined to the issue whether this loss was objectively likely to occur in the ordinary course of things. There is also the question whether, having regard for the commercial background of that party's undertaking, against which the parties contracted, the ordinary band of responsibility should be narrowed or expanded. As we shall see in the quotations set out below, Toulson LJ is suggesting (1) that the parties' dealings might restrict liability so that it does not cover any or all the relevant loss, even if that loss falls within the band of ordinary likelihood; (2) or, conversely, the zone of responsibility might be expanded to include quite freakish losses (as on the facts of the *Supershield* case, where the defendant was very 'unlucky' that back-up systems serially failed). Application of (1) and (2) requires the court to make a sensible assessment of the tacit understanding reasonably imputable to parties, judged at the time of the contract's formation. It seems better to place all these matters under the same rubric of 'remoteness' rather than to split the inquiry into two distinct, and forensically successive, tests of remoteness and scope of duty.

Toulson LJ in the *Supershield* case (2010) considered both Lord Hoffmann's seminal speech in *South Australia Asset Management Corp. v. York Montague Ltd* (1997),²⁴⁶ where the scope of duty test was first enunciated, and Lord Hoffmann's observations on that same test in the *Transfield* case (2008). Toulson LJ said:²⁴⁷

In *Transfield Shipping* (2008) ... the House of Lords held that the damages recoverable by the owners were limited to the period of overrun and should not include any subsequent loss. Lord Rodger and Baroness Hale reached that conclusion on the ground that the subsequent loss was not an ordinary consequence of the breach, applying the rule in *Hadley v. Baxendale*. Lords Hoffmann and Hope took a broader approach. Developing the theme of his speech in *South Australia*, Lord Hoffmann said (at 24–25) that the rule in *Hadley v. Baxendale*, as explained in *The Heron II*, is not inflexible; it is intended to give effect to the presumed intention of the parties and not to contradict them. Although the arbitrators had found as a fact that the owner's loss after redelivery was foreseeable, the question whether that loss was one for which the charterer assumed contractual responsibility involved the interpretation of the contract as a whole against its commercial background ... Lord Walker in the *Transfield* case (2009) said (at 69) that it may be that the rather precise formulation of the notion of 'assumption of responsibility' applies (if at all) to cases within the second limb, but that the underlying idea – what was the common basis on which the parties were contracting? – applies to the rule as a whole. He also said (at 78) that

245 [2010] EWCA Civ 7; [2010] NPC 5, at [37].

246 [1997] AC 191, 212, HL, *per* Lord Hoffmann.

247 [2010] EWCA Civ 7; [2010] NPC 5, at [42].

The Heron II shows that the question is not simply one of probability, but of what the contracting parties must be taken to have had in mind, having regard to the nature and object of their business transaction, and he expressed agreement (at 87) with the reasons given by Lords Hoffmann, Hope and Rodger.

Toulson LJ concluded:²⁴⁸

Hadley v. Baxendale remains a standard rule but it has been rationalised on the basis that it reflects the expectation to be imputed to the parties in the ordinary case, i.e. that a contract breaker should ordinarily be liable to the other party for damage resulting from his breach if, but only if, at the time of making the contract a reasonable person in his shoes would have had damage of that kind in mind as not unlikely to result from a breach. However, *South Australia* and *Transfield Shipping* are authority that there may be cases where the court, on examining the contract and the commercial background, decides that the standard approach would not reflect the expectation or intention reasonably to be imputed to the parties. In those two instances the effect was exclusionary [and so operated to narrow the defendant's zone of responsibility]; the contract breaker was held not to be liable for loss which resulted from its breach although some loss of the kind was not unlikely. But logically the same principle may have an inclusionary effect [and so operate to increase the defendant's zone of responsibility]. If, on the proper analysis of the contract against its commercial background, the loss was within the scope of the duty, it cannot be regarded as too remote, even if it would not have occurred in ordinary circumstances.

Writing in the *Edinburgh Law Review* (2010), Lord Hoffmann has since commented as follows on his approach in the *Transfield* case:²⁴⁹

[T]he key to understanding the principles of remoteness of damage in contract [involves this] question ... what obligation to make compensation for breach of contract would a reasonable observer understand the contracting party to have undertaken? In the ordinary way, that will be compensation for any loss which the parties would reasonably have regarded as likely to flow from the breach. But there may be cases in which a reasonable man would consider that a greater or lesser obligation was being accepted.

This statement is consistent with the passage quoted from Toulson LJ in the *Supershield* case (2010) (see above).

- 18.44** *Other illuminating decisions on contractual remoteness.* The next group of cases sheds light on aspects of the test.

²⁴⁸ *Ibid.*, at [43].

²⁴⁹ (2010) 14 *Edinburgh Law Review* 47, 55.

- (1) ‘*Ordinary course of things*’. *Balfour Beatty Construction Ltd v. Scottish Power* (1994)²⁵⁰ shows that, in the absence of special knowledge, a utility cannot be rendered liable for economic loss flowing from the claimant’s specialist activities because such vulnerability cannot be imputed to the defendant in the ordinary course of business. The pursuers were the main contractors responsible for building part of a motorway in Edinburgh. The works included construction of an aqueduct. This required a continuous flow of cement, which in turn presupposed that the defendants would continue to supply electricity. The defendant had agreed to supply a temporary special electricity point. But the supply failed. This was a breach of contract. As a result, cement ceased to flow, and the aqueduct became leaky. The pursuers (reasonably) chose to rebuild it. They claimed the cost of these remedial works. The claim foundered as too remote: the defendant could not reasonably be expected to have foreseen this physical catastrophe (applying the first limb of the test). Nor was special knowledge of the pursuer’s peculiar reliance on the continuous flow of electricity brought to the defendant’s attention, for the purpose of limb 2 of the *Hadley v. Baxendale* test. Lord Jauncey said:

When the activity of A involves complicated construction or manufacturing techniques, I can see no reason why B who supplies a commodity that A intends to use in the course of those techniques should be assumed ... to be aware of the ... effect thereupon of any failure of or deficiency in that commodity.²⁵¹

- (2) ‘*Special information*’. On this issue, Lord Walker said in *Jackson v. Royal Bank of Scotland plc* (2005)²⁵² that the criterion is ‘the extent of the shared knowledge of both parties when the contract was made ... including the possibility that knowledge of the defendant alone is enough’. And Waller LJ said in *Mulvenna v. Royal Bank of Scotland plc* (2003):²⁵³ ‘[S]imply drawing the attention of the [defendant] to special circumstances, does not necessarily impose a liability on the [defendant] to be responsible for damages flowing from [those] special circumstances.’ And he cited *McGregor on Damages*:²⁵⁴ ‘[The parties must] contemplate that the defendant is taking the risk of being liable for such consequences should they occur.’
- (3) *Overlapping claims in tort and contract*. *Brown v. KMR Services Ltd* (1995)²⁵⁵ concerned claims by Lloyd’s names against their members’ agents for breach of contract and negligence. The defendants contended that the size of the losses in the

250 1994 SLT 807; *The Times*, 23 March 1994, HL (Sc) (Scots case on appeal to the House of Lords); H. MacQueen, [1996] *Juridical Review* 295; A. Burrows, *Understanding the Law of Obligations* (Oxford, 1998), 160 ff.

251 1994 SLT 807, 810 HL (Sc).

252 [2005] 1 WLR 377, HL, at [49], citing *Kpohraror v. Woolwich Building Society* [1996] 4 All ER 119, 127–8, *per* Evans LJ; A. S. Burrows, *Remedies for Torts and Breach of Contract* (3rd edn, Oxford, 2004), 85–6.

253 [2003] EWCA Civ 1112, at [24] and [25], Waller LJ (the other judges agreeing).

254 *McGregor on Damages* (18th edn, London, 2009), 6–199.

255 [1995] 4 All ER 598, CA; A. S. Burrows, in A. S. Burrows and E. Peel (eds.), *Commercial Remedies: Current Issues and Problems* (Oxford, 2003), 34–6.

relevant years was so catastrophic that it was both unforeseeable in tort and too remote in contract. The Court of Appeal disagreed and treated the type of loss as foreseen and contemplated for the purpose of the *Hadley v. Baxendale* rule, and so not too remote.²⁵⁶ The *Brown* case (1995) appears to establish that economic loss – on the facts, exposure to insurance losses – caused by breach of contract – as distinct from loss of profits – need only be contemplated as a head of loss: it is unnecessary to contemplate the extent of that economic loss. This extends the approach of Orr and Scarman LJ in the *Parsons* case (see 18.43 case (4)). Burrows contends that the *Brown* case might be interpreted as deciding that the contract test should apply to both the contractual and tortious claims when there is a business relationship between the parties giving rise to overlapping obligations in contract and tort.²⁵⁷

- 18.45 ‘*Scope of duty*’ criterion. For the argument that the scope of duty test should be abandoned for contractual damages claims and that this factor can be adequately subsumed within the test of remoteness, see 18.43. The House of Lords in *Banque Bruxelles Lambert SA v. Eagle Star Insurance Co. Ltd* (the *SAAMCO* case) (1997)²⁵⁸ applied this test in the context of a surveyor’s negligent valuation of property. This concept sets a limit upon a person’s responsibility for loss when (a) the basic head of claim is directly attributable to his breach and is recoverable but (b) that loss has become aggravated by a fall in the market price of the relevant subject matter. Only the loss at (a) is recoverable, according to the House of Lords in the *Banque Bruxelles/SAAMCO* case.

The problem of the ‘market fall’ arises as follows. X wishes to lend to Y against the security of Y’s commercial property, and D is hired by X to value Y’s property. D values the property at £10m. In fact, the property’s true market value at that date is only £5m. D has been negligent in making this false valuation. If the property subsequently falls to £2m, because of a property slump, and if the property is the only source of repayment of Y’s debt, is D liable to X for £8m or only £5m? The House of Lords restricted D’s loss to £5m: D does not impliedly undertake to protect X against subsequent market fluctuations but is merely giving a valuation effective at that date.

As Lord Hoffmann said in the *Banque Bruxelles/SAAMCO* case:

[A] valuer provides an estimate of the value of the property at the date of the valuation. He does not undertake the role of a prophet. It is unfair that merely because for one reason or other the lender would not otherwise have lent, the valuer should be saddled with the whole risk of the transaction, including a subsequent fall in the value of the property.²⁵⁹

256 [1995] 4 All ER 598, 620–1, 642–3, CA.

257 A. S. Burrows and E. Peel (eds.), *Commercial Remedies: Current Issues and Problems* (Oxford, 2003), 35; and A. S. Burrows, *Remedies for Torts and Breach of Contract* (3rd edn, Oxford, 2004), 93–4; cf Bingham MR in the *Banque Bruxelles Lambert* case, [1995] QB 375, 405E, CA (cited in the text at 18.47).

258 *Banque Bruxelles Lambert SA v. Eagle Star Insurance Co. Ltd* (the ‘SAAMCO’ case) [1997] AC 191, HL.

259 *Ibid.*, at 210, HL.

And so the defendant's liability is merely the difference in the stated and real values at that date. The subsequent fall in value lies outside the 'scope' of the defendant's obligation. He is not warranting that the property's value will not fall subsequent to his valuation.

18.46 When will the scope of duty test apply? It is no longer confined to professional negligence cases. The test has been considered in the context of a suicidal employee²⁶⁰ and the voluntary undertaking by a bookmaker to deny the claimant a telephone betting account.²⁶¹ And, as we have seen in the discussion of the *Transfield* case (2008) (18.43 case (5)), Lord Hoffmann applied this concept to deny a ship-owner damages for loss of an attractive 'follow-on' charterparty.²⁶² But, in the *Transfield* case (2008), Baroness Hale considered that the scope of duty test might engender commercial uncertainty if applied generally and beyond the context of professional negligence in which it was first applied (18.43 case (5)). There is good sense in her plea to resist over-enthusiastic resort to this restrictive device. She said:²⁶³ 'Questions of assumption of risk depend upon a wider range of factors and value judgments. This type of reasoning ... could easily be at the expense of justice in some future case. It could also introduce much room for argument in other contractual contexts.' As suggested above, perhaps the true view is that the *Hadley v. Baxendale* principle is pliable enough to include consideration of the transaction's background and allocation to the parties of appropriate levels of responsibility for the consequences of breach of a particular obligation. This was Lord Walker's suggestion in the *Transfield* case. This idea is further suggested by Toulson LJ in *Supershield*.²⁶⁴ The scope of duty test is an attempt to fix the parties' joint assumption concerning the limits of the relevant party's compensatory responsibility. If so, the principle of 'Occam's Razor' requires that the scope of duty test would not be used in tandem with the *contractual test of remoteness*; instead, it should be used only to supplement the *different remoteness test in tort* (based upon liability for all consequences, provided only they are reasonably foreseeable: see 18.42 above on the *Wagon Mound* test).

18.47 Indeed, the 'need' for the scope of duty test would vanish in the context of 'professional negligence' cases if the governing test of remoteness were the *Hadley v. Baxendale* principle, and if resort to the *Wagon Mound* test (the criterion of reasonable foreseeability adopted in the tort of negligence) were disapplied in that context. As we have seen (18.44), Burrows suggests that *Brown v. KMR Services Ltd* (1995)²⁶⁵ might be interpreted as deciding that the contract test should apply to both the contractual and

260 E.g. *Corr v. IBC Vehicles Ltd* [2008] UKHL 13; [2008] 2 All ER 943, at [9] and [10].

261 *Calvert v. William Hill Credit Ltd* [2008] EWCA Civ 1427; [2009] Ch 330, at [46] and [47]: citing at [43] ff Lord Hoffmann's discussion of 'Causation' in (2005) LQR 592.

262 [2008] UKHL 48; [2009] 1 AC 61 (Lord Hoffmann, Lord Hope supported this approach; Lord Walker at [87] approved it, but his own reasons were based on the 'remoteness analysis').

263 *Ibid.*, at [93], per Baroness Hale.

264 [2010] EWCA Civ 7; [2010] NPC 5, at [37].

265 [1995] 4 All ER 598, CA; A. S. Burrows, in A. S. Burrows and E. Peel (eds.), *Commercial Remedies: Current Issues and Problems* (Oxford, 2003), 34–6.

tortious claims when there is a business relationship between the parties giving rise to overlapping obligations in contract and tort.²⁶⁶ If this point had been earlier acknowledged, there would have been no need for Lord Hoffmann (with the concurrence of the other members of the House of Lords) to have invented the ‘scope of duty’ cut-off device if the Court of Appeal in the *Banque Bruxelles/SAAMCO* case had held that the element of loss attributable to ‘market fall’ was a type of economic loss not recoverable as contractual damages because this risk was not in the contemplation of the parties, applying the *Hadley v. Baxendale* principle. Instead, the Court of Appeal’s judgment in the *Banque Bruxelles/SAAMCO* case on this point is bland (the result, it seems, of counsel’s concession that *Wagon Mound* remoteness applied to these facts).²⁶⁷ In short, the applicable test should have been *contractual remoteness* (as distinct from tortious remoteness). That tool would have been adequate for the task of restricting the surveyor’s liability.

- 18.48 *Damages to reflect post-breach events.* The House of Lords decision in *Golden Strait Corporation v. Nippon Yusen Kubishika Kaisha* (*‘The Golden Victory’*) (2007) makes clear that assessment of damages should reflect post-breach facts *if they are already known and they would have had the effect of diminishing the claimant’s loss.*²⁶⁸

In December 2001, a charterer had repudiated the contract by returning the ship early (contract to run for seven years from 1998). The question was whether damages (which fell to be assessed as from 2001) should reflect the fact that the contract would have been terminated, without breach, by the charterer subsequently invoking a war clause. It was clear (as found by the arbitrator) that the charterer would have so cancelled the contract once war was declared between the USA and Iraq in March 2003.

A majority of the House of Lords,²⁶⁹ upholding the Court of Appeal, held that it would be unjust not to take account of these supervening events when assessing the damages. They rejected the concept that the innocent party’s right to compensation is to be worked out without regard to these subsequent events. The outbreak of war would have entitled the charterer to invoke the war clause. From that point, the charterer would have been absolved from contractual liability to pay hire. In the majority’s opinion, damages must reflect this hindsight; to fail to do so would involve ‘over-compensation’.

266 A. S. Burrows, in A. S. Burrows and E. Peel (eds.), *Commercial Remedies: Current Issues and Problems* (Oxford, 2003), 35; and A. S. Burrows, *Remedies for Torts and Breach of Contract* (3rd edn, Oxford, 2004), 93–4; cf Bingham MR in the *Banque Bruxelles Lambert* case, [1995] QB 375, 405E, CA, passage cited in the text at next note (a terse attempt to elide tort and contract on this point, without citation of authorities).

267 *Banque Bruxelles Lambert* case, [1995] QB 375, 405, CA.

268 [2007] UKHL 12; [2007] 2 AC 353; noted by M. Mustill, (2008) 124 LQR 569–85; J. Morgan, [2007] CLJ 263; C. Nicholls, [2008] JBL 91; B. Coote, (2007) 123 LQR 503; Sir Bernard Rix, ‘Lord Bingham’s Contributions to Commercial Law’, in M. Andenas and D. Fairgrieve (eds.), *Tom Bingham and the Transformation of the Law: A Liber Amicorum* (Oxford, 2009), at 679–83.

269 Lords Scott, Carswell and Brown (dissents by Lords Bingham and Walker).

Peel,²⁷⁰ Treitel,²⁷¹ Reynolds,²⁷² Morgan²⁷³ and Coote²⁷⁴ say that this decision is unattractive, first, because it introduces ‘unwelcome uncertainty’, and, secondly, because it discourages settlement of the claim at the time of the breach. Furthermore, writing extra-judicially, Lord Mustill has criticised the majority decision as conceptually incoherent because it overrides the established view that, when an anticipatory breach occurs, and the innocent party elects to terminate the contract, damages are to be worked out at that date of termination.²⁷⁵ ‘[T]he valuation of the [promisee’s] lost rights should be performed as at the date of the acceptance [of the other party’s renunciation].’ However, Burrows approves the majority’s decision, suggesting that the chronological starting point for assessment of damages should be, and in his opinion has become, the date of judgment at trial.²⁷⁶ Liu also supports the majority’s decision.²⁷⁷

- 18.49 *Mitigation of damage principle.*²⁷⁸ The claimant must take reasonable steps to mitigate his loss, either by reducing or even by eliminating that loss. If mitigation efforts are successful, the defendant’s liability is adjusted accordingly; and, if there is a failure to mitigate, to that extent damages will also be reduced. Thus, in the *British Westinghouse* case (1912), Viscount Haldane LC said:

[This principle] imposes on a plaintiff the duty of taking all reasonable steps to mitigate the loss consequent on the breach and debars him from claiming any part of the damage which is due to his neglect to take such steps.²⁷⁹

The mitigation principle will now be elaborated.

270 Treitel (12th edn, London, 2007), 20-071.

271 G. H. Treitel, (2007) 123 LQR 9, 17.

272 F. M. B. Reynolds, ‘“The Golden Victory” – A Misguided Decision’ (2008) HKLJ 333.

273 J. Morgan, [2007] CLJ 263, 264–5.

274 B. Coote, (2007) 123 LQR 503, 510.

275 M. Mustill, (2008) 124 LQR 569, 584.

276 A. S. Burrows, in M. Andenas and D. Fairgrieve (eds.), *Tom Bingham and the Transformation of the Law: A Liber Amicorum* (Oxford, 2009), 598–601 (preferring the date of judgment approach adopted by Oliver J in *Radford v. De Froberville* [1977] 1 WLR 1262 and by Lord Wilberforce in *Johnson v. Agnew* [1980] AC 367, HL; Burrows also citing his more detailed discussion of this topic in A. S. Burrows, *Remedies for Torts and Breach of Contract* (3rd edn, Oxford, 2004), 188 ff, and opposing S. Waddams, ‘The Date for the Assessment of Damages’ (1981) 97 LQR 445).

277 [2007] LMCLQ 273.

278 A. S. Burrows, *Remedies for Torts and Breach of Contract* (3rd edn, Oxford, 2004), 122–8; M. Bridge, ‘Mitigation of Damages in Contract and the Meaning of Avoidable Loss’ (1989) 105 LQR 398; M. Bridge, ‘The Market Rule of Damages Assessment’, in D. Saidov and R. Cunnington (eds.), *Contract Damages: Domestic and International Perspectives* (Oxford, 2008), chapter 18; H. McGregor, ‘The Role of Mitigation in the Assessment of Damages’, in D. Saidov and R. Cunnington (eds.), *Contract Damages: Domestic and International Perspectives* (Oxford, 2008), chapter 14; for comparative sources, see G. H. Treitel, *Remedies for Breach of Contract* (Oxford, 1988), [145] ff; *Principles of European Contract Law*, Article 9:505, and UNIDROIT’s *Principles of International Commercial Contracts*, Article 7.4.8; and the (abortive) *Contract Code: Drawn up on Behalf of the English Law Commission* (Milan, 1993), section 439.

279 [1912] AC 673, 689, HL; e.g. house-owner had not acted unreasonably in refusing to allow the builder to effect repairs: *Iggleden v. Fairview New Homes (Shooters Hill) Ltd* [2007] EWHC 1573 (TCC), Coulson J.

Duty to endeavour to reduce or eliminate loss

The main mitigation rule is that an innocent party is expected to take reasonable steps to reduce or eliminate the loss caused by, or likely to ensue from, the other party's breach of contract (or tortious misconduct). 'Reasonable steps' do not require a claimant to engage in litigation,²⁸⁰ unless that course is exceptionally predictable and risk-free (as for this proviso, see *Western Trust & Savings Ltd v. Travers & Co.* (1997) and *Walker v. Geo H Medlicott* (1999), both mentioned below). Certainly, the claimant is not required to sue third parties if this will injure its commercial reputation.²⁸¹

In *Pilkington v. Wood* (1953), Harman J held that the claimant had not failed to mitigate his loss on these facts. The claimant had bought a house from T, but it turned out that T's title was defective. The purchaser's solicitor, the defendant in this case, had been negligent in failing to discover the defect in title. The defendant contended that the claimant might have avoided its loss by suing T for failure to show a good title. Harman J said that such litigation would have involved 'no little difficulty' and might not necessarily have succeeded. Accordingly, the claimant had failed to satisfy the mitigation principle, even taking into account the defendant solicitor's willingness to indemnify the claimant for the costs of the litigation against T. Harman J concluded as follows on this point:²⁸²

[T]he so-called duty to mitigate does not go so far as to oblige the injured party, even under an indemnity, to embark on a complicated and difficult piece of litigation against a third party ... to protect his solicitor from the consequences of his own carelessness.

However, sometimes a commercial party might be reasonably expected to pursue litigation. Thus, in *Western Trust & Savings Ltd v. Travers & Co.* (1997), the Court of Appeal held that, in satisfaction of the mitigation principle, mortgage lenders should have sought a possession order against a third party.²⁸³ And even non-commercial parties might sometimes be expected to engage in formal proceedings against third parties. Thus, in *Walker v. Geo. H Medlicott* (1999), the Court of Appeal considered the context where a lawyer has failed to execute properly the client's instructions for executing a will. Here, the court held that disappointed prospective legatees would fail to mitigate loss arising from such professional negligence if they did not pursue the 'primary' route by seeking judicial rectification of the will.²⁸⁴ These cases were considered by Mummery LJ in *Horsfall v. Haywards* (1999).²⁸⁵

The defendant bears the burden of proving that there has been a failure to mitigate.²⁸⁶ Furthermore, the question whether a party has satisfied the mitigation

280 *Pilkington v. Wood* [1953] Ch 770, Harman J.

281 *James Finlay & Co. v. Kwik Hoo Tong* [1929] 1 KB 400, CA; *London and South of England Building Society v. Stone* [1983] 3 All ER 105, CA.

282 [1953] Ch 770, 777, Harman J.

283 [1997] PNLR 295, CA.

284 [1999] 1 All ER 685, CA (application for rectification of a will under section 20 of the Administration of Justice Act 1982).

285 [1999] PNLR 583, 588, CA.

286 *Geest plc v. Lansiquot* [2002] UKPC 48; [2002] 1 WLR 3111, PC; *Roper v. Johnson* (1873) LR 8 CP 167, 178, 181–2.

principle is treated as an issue of fact, which appellate courts are highly unlikely to disturb.²⁸⁷

Unproblematic examples

- (1) *Wrongful dismissal*. An employee who is wrongfully dismissed cannot use the defendant's liability to pay compensation for loss arising from this breach as a 'bread-ticket'. Instead, the claimant must try to re-enter the jobs market. There will be no failure by the employee to mitigate his loss when an offer of new employment involves an unreasonable diminution of his status and conditions. For example, in *Shindler v. Northern Raincoat Co. Ltd* (1960), a senior manager did not have to suffer the indignity of appointment at a lower rank.²⁸⁸ Subject to that, sometimes the responsibility to attempt a reasonable mitigation of loss requires the innocent party to accept an offer of re-employment with the defendant, as stated in *Brace v. Calder* (1895).²⁸⁹
- (2) *Sale of goods: failure to supply or purchase*. The assumption is that the innocent party can resell to a third party or repurchase from a third party, thereby mitigating his loss, provided there is an 'available market' for such goods. Thus, a seller or buyer (respectively), when suing for damages for non-acceptance of goods or non-delivery, should recover *prima facie* the difference between the price agreed and the (higher) market value of substitute goods, these differences in amounts to be calculated at the date of agreed delivery or, if no such date was agreed, the date of breach.²⁹⁰
- (3) *Sale of goods: no obligation to mitigate by accepting shoddy or inferior goods*. In *Heaven & Kesterton Ltd v. Etablissements Francois Albiac et Cie* (1956), the seller had tendered timber of inferior quality.²⁹¹ The buyer rejected it. Devlin J held that the mitigation principle did not require the buyer to accept these shoddy goods.

Two problematic cases²⁹²

- (1) *Sale of goods: buyer not justified in rejecting seller's revised payment terms*. In *Payzu Ltd v. Saunders* (1919), the defendant agreed to sell *crêpe de chine* (a fabric) in lots. The buyer agreed that he would pay for each delivery within one month of receipt, but not necessarily in cash.²⁹³ The buyer paid late for the first consignment. The

287 E.g. *The Solholt* [1983] 1 Lloyd's Rep 605, CA (and earlier the *Payzu* case, [1919] 2 KB 581, CA, examined in the text in the present paragraph, below).

288 [1960] 1 WLR 1038, Diplock J; *Yetton v. Eastwoods Froy Ltd* [1967] 1 WLR 104, 118C–D, 119D (no default in mitigation), Blain J, reviewing the case law.

289 [1895] 2 KB 253, CA.

290 Sections 50(3) and 51(3) of the Sale of Goods Act 1979.

291 [1956] 2 Lloyd's Rep 316, Devlin J (appropriateness of such a rejection now subject to section 15A of the Sale of Goods Act 1979 (17.35) if the basis of the termination were a breach of an implied statutory term concerning quality).

292 H. McGregor, 'The Role of Mitigation in the Assessment of Damages', in D. Saidov and R. Cunnington (eds.), *Contract Damages: Domestic and International Perspectives* (Oxford, 2008), chapter 14, at 335.

293 [1919] 2 KB 581, CA (cf vendor in breach of contract; no vacant possession; property occupied by a sitting tenant; no duty to accept vendor's offer of repurchase of real property: *Strutt v. Whitnell* [1975] 1

seller, wrongly inferring that the buyer was close to insolvency, insisted on cash payment for future deliveries. But the buyer did not accept this revision. Instead, the buyer chose to terminate the contract by reason of the seller's repudiation. The buyer sued for damages, namely, the difference between the market price and the contract price, the market having risen. The Court of Appeal held that the buyer should have accepted the seller's revised terms of business, that is, the new offer to continue the contractual deliveries, in return for cash payments. The buyer's decision not to continue relations was a failure to mitigate his loss. Therefore, his damages were confined to £50, representing the period of credit which the buyer would have lost by paying cash on delivery rather than when stipulated by the contract. The decision is surprising because the court's application of the mitigation principle here denied the buyer the right to terminate. The seller had failed to adhere to the original terms of payment, and the difference between cash payment (as now insisted on, wrongly) and credit terms is of great commercial significance (compare the facts of the *CTN Cash & Carry* case:²⁹⁴ 11.09).

- (2) *Sale of goods: buyer's rejection when ship delivered three days late.* In *'The Solholt'* (1983), the seller agreed to sell a vessel to the buyer for US\$5m by 31 August.²⁹⁵ However, the seller breached the contract by proposing to make delivery three days late, on 3 September. This was a repudiatory breach, on which basis the buyer justifiably terminated the contract. At the date of termination, the vessel's value had already increased 10 per cent to US\$5.5m. The buyer tried to buy the vessel for US\$4.75m, but the seller did not accept. The trial judge, Staughton J, found as a fact that the seller would have been prepared to sell under a renewed contract to the buyer for US\$5m, and, furthermore, he also held that it would have been reasonable for the buyer to have accepted that offer. Instead, the seller sold the vessel to a third party for US\$5.8m.²⁹⁶ The Court of Appeal upheld Staughton J's decision that the buyer's failure to seek delivery under a revised contract at US\$5m was an unreasonable failure to mitigate. The decision in *'The Solholt'* (1983) goes further than the *Payzu* case (1919) (see above) because, in that earlier case, the possibility of continuing relations had been expressly suggested by the vendor in breach (subject to cash payments), whereas no such suggestion had been made by the guilty vendor in *'The Solholt'* (1983) (no offer to sell the ship for a reduced price). Furthermore, *'The Solholt'* nullifies the buyer's ordinary right to compensation arising from his justified termination of the contract for repudiatory breach (late delivery). Michael Bridge contends that the buyer should have been entitled to the initial 10 per cent

WLR 870, CA; approved by M. Bridge, (1989) 99 LQR 398, 422–3; MacKenna J, the third appeal judge, distinguished the *Payzu* case as one where the buyer was not being forced to undo a transaction where property had already passed).

294 [1994] 4 All ER 714, CA.

295 [1983] 1 Lloyd's Rep 605, CA, noted by E. Lomnicka, (1983) LQR 495–7; cf *Sealace Shipping Co. Ltd v. Ocean Voice Ltd* [1996] 1 Lloyd's Rep 120, 125 CA (on which see *Ruxley Electronics and Construction Ltd v. Forsyth* [1996] 1 AC 344, 371H, HL; the latter case itself is also an example of a damages claim disproportionate to the innocent party's true loss).

296 As suggested by the trial judge, noted by M. Bridge, (1989) 105 LQR 398, 418.

increase in the ship's value (US\$500,000)²⁹⁷ as a 'loss of bargain' which had already arisen. That claim should not have been nullified by the buyer's alleged 'mitigation' failure. As for the additional US\$300,000 gain achieved by the sale to the third party, Bridge suggests that the seller should be entitled to keep this gain. This is because the buyer had already abandoned interest in this ship at the time this further increase in value occurred.

Mitigation in face of hazardous breach

The following propositions (supported by the cases examined below) have emerged:

- (1) The mitigation principle only applies if a claimant fails to take appropriate precautions after he has become aware of a probable breach of contract which creates a serious hazard.
- (2) Awareness that something is significantly wrong is enough; precise and certain knowledge of the other party's breach is not required.
- (3) But the claimant cannot owe a duty to mitigate if he was ignorant of the breach (see *Schering Agrochemicals Ltd v. Resibel NVSA* (1992)²⁹⁸ and *County Ltd v. Girozentrale Securities* (1996), both examined in detail in the text immediately below).²⁹⁹

In *Schering Agrochemicals Ltd v. Resibel NVSA* (1992), the defendant supplied bottle-sealing machinery to the claimant, together with a safety alarm system.³⁰⁰ The bottles contained highly explosive material. They had to be kept moving along the processing belt. Otherwise, they would be exposed to excessive heat. But the claimant's bottling system was faulty. It failed to stop the heat-sealing process when the bottles were stationary for too long. Although this defect had been reported to the claimant by its staff, its management took no action and continued to use the machinery. Some time later, the machine blew up, causing a fire. The claimant sued the defendant for damage to his factory. The Court of Appeal unanimously held, but for different reasons, that the defendant was not liable for the fire damage. Nolan LJ (with whom Purchas LJ agreed) held that the claimant had failed to mitigate. The claimant's decision to ignore the defect was reckless. The defendant's supply of defective equipment was a breach³⁰¹ which created a serious hazard. Once the claimant became aware of the hazard, the mitigation principle rendered it prudent that the claimant take all sensible safety precautions.³⁰² (The third judge, Scott LJ, denied recovery on the basis of remoteness; but his reasoning was rightly repudiated in another case.)³⁰³

297 M. Bridge, (1989) 105 LQR 398, 417.

298 Court of Appeal, 26 November 1992, unreported, Court of Appeal transcript No. 1298 of 1992, noted by A. S. Burrows, (1993) 109 LQR 175.

299 *County Ltd v. Girozentrale Securities* [1996] 3 All ER 834, CA.

300 Court of Appeal, 26 November 1992, unreported, Court of Appeal transcript No. 1298 of 1992.

301 Section 14(3) of the Sale of Goods Act 1979.

302 Approved by A. S. Burrows, (1993) 109 LQR 175, 176 (but advocating wider statutory power to apportion responsibility according to relative fault: see 18.50).

303 *County Ltd v. Girozentrale Securities* [1996] 3 All ER 834, 858H, CA.

In the case just discussed, the defendant's breach was manifest. It was different in *County Ltd v. Girozentrale Securities* (1996), where the Court of Appeal affirmed that no duty to mitigate arises unless and until the claimant is aware of either a manifest or a possible breach.³⁰⁴

In *County Ltd v. Girozentrale Securities* (1996), the claimant bank had agreed to underwrite the issue of 6 million shares in R plc, a quoted company. The defendant stockbrokers had arranged to approach potential investors to place these shares. But many of the defendant's proposed investors failed to materialise. As a result, a substantial number of the shares were not taken up. This exposed the claimant bank to a loss of almost £7m. The defendant brokers contended that the claimant should have checked the reliability of the proposed investors' interest in buying the shares. But the Court of Appeal rejected this. At this stage, the claimant had been completely unaware that the defendant had breached its contract.³⁰⁵ And so it was premature to attribute any duty of mitigation at this early phase. When the claimant did become aware of the breach, it acted sensibly.³⁰⁶ Prior to that, it would have been unreasonable, and wrong in principle, to expect the claimant to double-check its professional advisor's market testing.

Recovery of extra loss for successful or unsuccessful attempt to mitigate

The innocent party is entitled to recover from the defendant any expense or additional loss incurred when taking reasonable steps to mitigate the loss.³⁰⁷ Such loss is recoverable even if the attempt at mitigation was unsuccessful, provided this attempt was reasonable.³⁰⁸

In *Banco de Portugal v. Waterlow & Sons Ltd* (1932),³⁰⁹ the defendant was commissioned by the claimant bank to print bank notes in a new issue of Portuguese currency. The defendant breached its contract by allowing thousands of these new notes to fall into the hands of an international criminal who fraudulently put them into circulation. The House of Lords held, by a majority, that the claimant bank had acted reasonably in buying up these notes and cancelling this issue. These steps were commensurate with the perilous situation created by the breach. Such loss was recoverable even though it was not foreseeable at the contract's commencement.

In *Holden Ltd v. Bostock & Co. Ltd* (1902),³¹⁰ the defendant sold sugar to the claimant for brewing purposes. But the sugar was contaminated with arsenic. The claimant incurred advertising expenditure to reassure customers that the danger of arsenic poisoning had now

304 *Ibid.*

305 *Ibid.*, at 859A–B, *per* Hobhouse LJ.

306 *Ibid.*, at 858F.

307 H. McGregor, 'The Role of Mitigation in the Assessment of Damages', in D. Saidov and R. Cunningham (eds.), *Contract Damages: Domestic and International Perspectives* (Oxford, 2008), chapter 14, at 336.

308 *Esso Petroleum Co. Ltd v. Mardon* [1976] QB 801, CA.

309 [1932] AC 452, HL.

310 (1902) 18 TLR 317.

been removed. It was held that this expense had been reasonably incurred in mitigation, and so it could be recovered.

But in *'The Borag'* (1981),³¹¹ the Court of Appeal refused to allow a claim for excessive interest charges incurred on a loan taken out by the claimant in order to finance the release of a ship detained in breach of contract. These high charges were not a reasonable act of mitigation.

Mitigation in fact achieved

The House of Lords in *British Westinghouse Electric Co. Ltd v. Underground Electric Railways* (1912) made clear that the innocent party must offset against his damages any benefits which in fact accrue to him as a result of steps taken by him in response to the relevant breach.³¹²

In *British Westinghouse Electric Co. Ltd v. Underground Electric Railways* (1912), the seller supplied defective turbines. The buyer decided to use alternative and superior turbines, which it bought from a third party supplier. This enterprising decision to invest in new technology enabled the buyer to operate much more profitably than it would have done even if the seller had supplied non-defective turbines. The buyer claimed two heads of loss: (1) the loss attributable to running the deficient machines before they were replaced; and (2) the cost of installing the new machines. Head (1) was unproblematic. But head (2) was, in the House of Lords' opinion, subject to the mitigation principle: for that loss had been eliminated by the economy achieved from using the new machines; and that commercial decision to find substitutes was a reasonable step taken by an innocent party in the course of business. In fact, the buyer's expenses in buying and installing the replacement machines were recouped readily by the extra profitability of the new machines.³¹³ Viscount Haldane LC said that the increase in the buyer's profitability as a result of installing the new machines 'was ... a natural and prudent course followed by those whose object was to avoid further loss, and ... it formed part of a continuous dealing with the situation in which they found themselves, and was not an independent or disconnected transaction.'³¹⁴ With this guidance, the case was remitted to the arbitrator.

But, in other cases, the courts have held that the claimant's unlocking of an eventual gain or saving, since not part of the process of mitigation, should not have the effect of reducing the claimant's compensation.³¹⁵ The lines of distinction are not clear-cut. The courts

311 [1981] 1 All ER 856, CA.

312 [1912] AC 673, 691, HL; subsequent cases reviewed in *Primavera v. Allied Dunbar Assurance plc* [2002] EWCA Civ 1327; [2003] PNL R 276, CA (on which see *McGregor on Damages* (18th edn, London, 2009), 7-130).

313 [1912] AC 673, HL.

314 *Ibid.*, at 691-2.

315 H. McGregor, 'The Role of Mitigation in the Assessment of Damages', in D. Saidov and R. Cunningham (eds.), *Contract Damages: Domestic and International Perspectives* (Oxford, 2008), chapter 14, at 336 ff.

have regard to: (1) the interval between the initial wrong and the claimant's subsequent benefit (the *Hussey* (1990) and *Gardner* (1997) cases: see the text below); (2) inconvenience or disruption to the claimant occurring during that interval; (3) the claimant's effort (including complex negotiations with third parties), determination, and ingenuity, in achieving that benefit; (4) whether the achievement of that benefit involved a deviation from the intended use of the subject matter of the relevant contract (real estate redeveloped, rather than use as a residence, as in the *Hussey* case); and (5) whether, as a matter of commercial prudence, it was appropriate for the innocent party to use a different product in the interest of achieving an economy (as in the *British Westinghouse* case).

In *Hussey v. Eels* (1990), in February 1984 the defendant sold a defective bungalow to the claimant,³¹⁶ the defendant having misrepresented that the property was free from subsidence. The claimant could not afford £17,000 to repair the property. And so the claimant obtained planning permission to construct two homes on the site, after demolishing the bungalow. Two years later, the site was sold, with the benefit of this planning permission, to a third party. This resale yielded a profit of £25,250. The claimant sought damages of £17,000, based on the difference in value, at the time of the original purchase, between the bungalow's actual value and the price paid. At first instance, the judge awarded nominal damages, offsetting the claimant's resale profit against this claim. But the Court of Appeal reversed this. It held that the resale could not be regarded as part of the claimant's responsibility to mitigate. Instead, this was a fresh event (however, Burrows regards this as unconvincing).³¹⁷ Mustill LJ explained:³¹⁸

[T]he plaintiff bought the [bungalow] to live in, and did live in it for a substantial period. It was only after two years that the possibility of selling the land and moving elsewhere was explored, and six months later still that this possibility came to fruition. It seems to me that when the plaintiffs unlocked the development value of their land they did so for their own benefit, and not as part of a continuous transaction of which the purchase of land and bungalow was the inception.

To echo Latham LJ's words in the *Primavera* case (2002),³¹⁹ the decision in the *Hussey* case to redevelop the land had merely an 'historical connection with' the defendant's initial misrepresentation. And the defendant could not take the benefit of the claimant's resourceful decision to extricate itself economically from the disastrous initial purchase.

In the *Gardner* case (1997), the defendant surveyor failed to spot structural defects in a maisonette which the claimant went on to buy on a long lease.³²⁰ The defects reduced the property's value by £85,000. Five years later, the claimant succeeded in requiring a third party,

316 [1990] 2 QB 227, 241 CA, *per* Mustill LJ, noted by A. J. Oakley, [1990] CLJ 394; *Primavera v. Allied Dunbar Assurance plc* [2002] EWCA Civ 1327; [2003] PNLr 276, CA.

317 A. S. Burrows, *Remedies for Torts and Breach of Contract* (3rd edn, Oxford, 2004), 160–1.

318 [1990] 2 QB 227, 241, CA, *per* Mustill LJ.

319 *Primavera v. Allied Dunbar Assurance plc* [2002] EWCA Civ 1327; [2003] PNLr 276, at [52].

320 *Gardner v. Marsh & Parsons (a firm)* [1997] 1 WLR 489, CA.

namely, his landlord, to repair the property, in compliance with his covenanted duty to repair. Hirst and Pill LJ (Peter Gibson LJ dissenting) considered that the defendant surveyor must pay £85,000 in compensation, even though the claimant had eventually achieved a complete repair without having himself to finance the work. Pill LJ, a member of the majority, said:³²¹

In my judgment, the present case, on its facts, is on the *Hussey v. Eels* side of the line ... The plaintiffs had to undertake protracted negotiations with that [freeholder] and ... the other tenants in the building. Before that obligation was performed by the freeholder, there was a considerable lapse of time in the course of which the plaintiffs, because of the structural defect, were unable to sell the property when they wished to do so.

But Peter Gibson LJ's dissent reveals the marginal nature of this decision: for, if the defendant surveyor and the third party landlord had been joined as co-defendants, and the latter's settlement offer had been accepted by the claimant, the court would not have granted damages for the same loss against the first defendant; to do so would flagrantly have infringed the principle that a party is not entitled to double or over-compensation. The more attractive approach would have been to award the claimant damages for its inconvenience suffered during the five-year period, including the 'hassle' of having to engage in such protracted negotiations with the third party landlord.

In *Harbutt's 'Plasticine' Ltd v. Wayne Tank & Pump Co. Ltd* (1970),³²² the Court of Appeal held that there should be no reduction in the claimant's damages (based on the 'cost of cure' measure), enabling the claimant to reconstruct its factory which had been destroyed as a result of the defendant's breach of contract (equipment supplied by the defendant had caused a catastrophic fire in the claimant's factory). There was no justification for reducing those damages to reflect the 'betterment' value of the new factory.

Similarly, in *Bacon v. Cooper (Metals) Ltd* (1982),³²³ the claimant received an award of damages enabling it to replace defective machinery. As a result, the claimant would obtain equipment having a longer life than the original machinery. Cantley J held, however, that no allowance should be made to reflect this improvement.

Link between the mitigation principle and 'cost of cure' damages

When deciding whether to award 'cost of cure' or reinstatement damages (on which see 18.27), the courts take into account whether it is reasonable to award that higher measure of damages, to finance a complete performance of the relevant promise, when compared with the sum which will reflect the claimant's economic loss.³²⁴ Conversely, where it is cheaper to repair rather than to replace, the mitigation principle will sometimes justify

³²¹ *Ibid.*, at 514.

³²² [1970] QB 447, CA.

³²³ [1982] 1 All ER 397, 400–2, Cantley J.

³²⁴ See 18.29 on *Ruxley Electronics and Construction Ltd v. Forsyth* [1996] 1 AC 344, HL; in *Radford v. De Froberville* [1977] 1 WLR 1262, 1268–88 (see 18.28), Oliver J explained the connection between decisions whether to award the reinstatement measure and the mitigation principle.

confining the innocent party to recovering the cost of cure measure of compensation rather than suing for the larger sum necessary to purchase a complete replacement.³²⁵

Mitigation principle does not apply to claim for debt

The mitigation principle concerns only claims for damages, and so it does not apply to a claim for debt. As explained at 18.05 ff (during discussion of the *White & Carter* case (1962)), the mitigation principle has no application when a party can freely elect not to terminate the contract and to 'accept' the other's renunciation, and instead he decides to complete his performance, charge the other party the agreed price, and so sue in debt (although the Supreme Court might usefully revisit this topic).

18.50 Claimant's 'contributory negligence' and the Law Reform (Contributory Negligence) Act 1945. Section 1(1) of the Act states:

Where any person suffers damage as the result partly of his own fault and partly of the fault of any other person or persons, a claim in respect of that damage shall not be defeated by reason of the fault of the person suffering the damage, but the damages recoverable in respect thereof shall be reduced to such extent as the court thinks just and equitable having regard to the claimant's share in the responsibility for the damage.

Fault is defined in section 4 as: 'negligence, breach of statutory duty or other act or omission which gives rise to a liability in tort or would, apart from this Act, give rise to the defence of contributory negligence'.

The defence of contributory negligence has little impact upon contractual claims for damages. This is because contributory negligence applies only where the relevant contractual obligation was (a) to exercise reasonable care (and many contractual obligations are *strict*), and (b) the relevant breach of contract has occurred within a relationship where the defendant *is also liable in the tort of negligence for the same default* (or, in other words, where there is 'concurrent' liability in contract and tort: see 1.23, 17.06). Proposition (a) reflects the wording of the 1945 Act. Proposition (b) was established in *Forsikringsaktieselskapet Vesta v. Butcher* (1989) (the *Vesta* case), where the Court of Appeal approved the following trichotomy noted by Hobhouse J, at first instance, in this case:³²⁶

The question whether the [Law Reform (Contributory Negligence) Act 1945] applies to claims brought in contract can arise in a number of classes of case.

(1) Where the defendant's liability arises from some contractual provision which does not depend on negligence on the part of the defendant.

³²⁵ *Ruxley Electronics and Construction Ltd v. Forsyth* [1996] 1 AC 344, 366 D, HL, Lord Lloyd.

³²⁶ *Forsikringsaktieselskapet Vesta v. Butcher* (affirmed on other points by the House of Lords, [1989] AC 852, 860, where the Court of Appeal's decision is also reported); Court of Appeal approving Hobhouse J at [1986] 2 All ER 488, 508.

(2) Where the defendant's liability arises from a contractual obligation which is expressed in terms of taking care (or its equivalent) but does not correspond to a common law duty to take care which would exist in the given case independently of contract.

(3) Where the defendant's liability in contract is the same as his liability in the tort of negligence independently of the existence of any contract.

In *Barclays Bank plc v. Fairclough Building* (1995), the Court of Appeal affirmed that the 1945 Act does not apply to a category (1) case (contractual strict liability).³²⁷ In the *Vesta* case, the Court of Appeal declared itself bound by earlier authority to confine the 1945 Act to category (3).³²⁸ It will be rare for a situation to fall within category (2) (stand-alone contractual duty of care) rather than category (3) (a concurrent contractual and tortious duties of care).³²⁹

In *Barclays Bank plc v. Fairclough Building* (1995),³³⁰ the defendant had been engaged to clean the roofs of the claimant bank's storage warehouse. The roofs were made of asbestos cement sheeting. The defendant failed to take proper precautions. As a result, its cleaning resulted in fibres falling into the warehouse. Remedial work to remove this contamination cost the claimant £4m. The defendant alleged that the claimant should have taken a stronger role in preventing this harm. The trial judge agreed and reduced damages by 40 per cent. But the Court of Appeal held that the 1945 Act was inapplicable because, using the *Vesta* threefold analysis, this was a category (1) case, that is, the defendant's contractual duty was strict. Nourse LJ said that the only possible defences on such facts were a release, waiver or forbearance (or, he might have added, absence of causation, or a problem of remoteness), but none of these could be sustained on the facts.

Four additional points should be noted. First, the 1945 Act does not apply to the action for deceit (9.12).³³¹ Secondly, the 1945 Act does apply to a claim for damages under section 2(1) of the Misrepresentation Act 1967 (9.14), provided the claimant enjoys a parallel common law action for negligence against the representor.³³² Thirdly, in contractual claims for negligent over-valuation of properties used by lenders as security, where the property price later falls because of market change, contributory negligence applies to the claimant's basic loss before it is cut down by the scope of duty test (see 18.45 on

327 [1995] QB 214, CA, noted by C. Hopkins, [1995] CLJ 20–3; A. S. Burrows, *Remedies for Torts and Breach of Contract* (3rd edn, Oxford, 2004), 136–44.

328 [1989] AC 852, 860, at 867F, CA, following *Sayers v. Harlow Urban District Council* [1958] 1 WLR 623, CA; *UCB Bank plc v. Heberd Winstanley & Pugh*, *The Times*, 25 August 1999, CA.

329 *Raflatac Ltd v. Eade* [1999] 1 Lloyd's Rep 506, Colman J; on the extensive incidence of overlapping contractual and tortious duties of care, see *Henderson v. Merrett Syndicates Ltd* [1995] 2 AC 145, HL (see 1.23).

330 [1995] QB 214, CA, noted by C. Hopkins, [1995] CLJ 20–3; A. S. Burrows, *Remedies for Torts and Breach of Contract* (3rd edn, Oxford, 2004), 136–44.

331 *Standard Chartered Bank v. Pakistan Corporation (Nos. 2 and 4)* [2003] 1 AC 959, HL, at [18], per Lord Hoffmann, and [42] to [45], per Lord Rodger.

332 *Gran Gelato Ltd v. Richliff Ltd* [1992] Ch 560, Nicholls V-C.

that test).³³³ Finally, it should be noted that contributory negligence is contemplated *even in respect of the primary wrongdoer's breach of a strict obligation* in the (non-binding) *Principles of European Contract Law*, Article 9:504, and UNIDROIT's *Principles of International Commercial Contracts* (2004), Article 7.4.7.³³⁴ This contrasts with English law, as explained above.

An uncontroversial suggestion for reform

Stand-alone contractual duty to take care. Burrows rightly regrets that the Law Commission's modest recommendation for extension of the 1945 Act's scope to category (2) (a 'stand-alone contractual duty of care') has not been implemented.³³⁵ This suggestion is clearly sound.

A deeply controversial suggestion for reform

Strict contractual obligation. But Burrows goes further and bemoans the absence of a percentage scale of possible discounting of damages in category (1) to take account of the claimant's culpable contribution to the harm resulting from breach of a strict undertaking or implied term.³³⁶ Extension of the contributory negligence defence to claims based on breach of strict contractual obligations had been recommended in 1990 in a Law Commission working paper, but the Law Commission resiled from this in its 1993 report. In its 1993 retreat, it had (attractively) considered that this would create uncertainty. It would also diminish consumers' bargaining strength if their claims for breach of strict obligations could be met by a defence of contributory negligence.³³⁷ Admittedly, Burrows is not persuaded by these objections.³³⁸ But his suggested change would be problematic, for the reasons stated by the Law Commission.

Lack of 'match' between claimant's contributory fault and the defendant's breach of a strict obligation

Burrows finds nothing incongruous in a breach of strict duty by the defendant being compared with a notional responsibility by the claimant not to contribute to the harm by carelessness or the like.³³⁹ In this last respect, he notes, first, that the *Principles*

333 *Platform Home Loans Ltd v. Oyston Shipways Ltd* [2000] 2 AC 190, HL; generally on the SAAMCO case, see 18.45.

334 2nd edn, Rome, 2004; see M. J. Bonell (ed.), *The UNIDROIT Principles in Practice: Case Law and Bibliography on the UNIDROIT Principles of International Commercial Contracts* (2nd edn, Ardsley, NY, 2006), 410–12; S. Vogenauer and J. Kleinheisterkamp (eds.), *Commentary on the UNIDROIT Principles of International Commercial Contracts* (Oxford, 2009), 897–900.

335 A. S. Burrows, *Remedies for Torts and Breach of Contract* (3rd edn, Oxford, 2004), 142–3, noting Law Commission, *Contributory Negligence as a Defence in Contract* (Law Commission Report No. 219, London, 1993).

336 A. S. Burrows, *Remedies for Torts and Breach of Contract* (3rd edn, Oxford, 2004), 141 ff; A. Porat, (1995) 111 LQR 228–34; A. Porat, 'A Comparative Fault Defence in Contract Law' (2009) 107 *Michigan Law Review* 1397–1412 (part of the symposium on 'Fault in American Contract Law').

337 Law Commission, *Contributory Negligence as a Defence in Contract* (Law Commission Working Paper No. 114, 1990); on the reasons for the Law Commission's change of mind, see C. Hopkins, [1995] CLJ 20, 22.

338 A. S. Burrows, *Remedies for Torts and Breach of Contract* (3rd edn, Oxford, 2004), 142–3.

339 *Ibid.*

of *European Contract Law*, Article 9:504, and UNIDROIT's *Principles of International Commercial Contracts* (2004), Article 7.4.7³⁴⁰ (21.02) allow contributory negligence to operate in category (1) cases. Secondly, he notes that the defence of contributory negligence also applies to certain strict liability torts under the Consumer Protection Act 1987, the Animals Act 1971 and the common law tort of nuisance established in *Rylands v. Fletcher*. Burrows also suggests that extension of this defence to breach of a strict contractual duty would avoid resort to the concept of causation which would operate harshly and involve an 'all-or-nothing' approach.³⁴¹

The objection to Burrows' suggestion is that contributory negligence involves an inquiry into the parties' respective contribution by misconduct or culpable default to the loss suffered. The defendant's breach of a strict obligation is not 'fault', in the sense of a failure to exercise due diligence, but a failure to comply with an express or implied promise to achieve a result: the claimant's fault and the defendant's breach are not *in pari materia*: like is not compared with like. Admittedly, as Burrows observes, the defence already applies to various 'strict' torts. But that might be the true anomaly. It is not obvious that one should fling open the door and apply this defence across the whole spectrum of contractual breaches, including the important strict obligations arising under commercial and consumer contracts, notably sale of goods.

Contributory negligence and uncertainty

The problem here is that extension of contributory negligence to all contractual breaches would inject an element of unpredictability. The resolution of such matters would become, as Burrows put it in 2004, 'complex disputes as to comparative blameworthiness'.³⁴² Overshadowing all contractual damages claims would be the prospect of an unpredictable percentage discount to reflect the claimant's alleged fault. Burrows' response to this problem is not quite convincing. He suggests³⁴³ that the court would be mandated to offer reductions of 25, 50 or 75 per cent. But a strong element of unpredictability would remain. And the open-ended nature of such disputes concerning contributory fault would also weaken consumer protection: for such a claimant, for example, the buyer of defective goods, confronted by an expanded defence of contributory negligence, might hesitate 'to hold out' until trial for full compensation, preferring to accept 25, 50 or 75 per cent, rather than the whole loaf.

Conclusion

For these reasons, it is submitted that contributory negligence should continue to be unavailable in *Vesta* category (1) (breach of a strict contractual obligation). It should

³⁴⁰ 2nd edn, Rome, 2004; see M. J. Bonell (ed.), *The UNIDROIT Principles in Practice: Case Law and Bibliography on the UNIDROIT Principles of International Commercial Contracts* (2nd edn, Ardsley, NY, 2006), 410–12; S. Vogenauer and J. Kleinheisterkamp (eds.), *Commentary on the UNIDROIT Principles of International Commercial Contracts* (Oxford, 2009), 897–900.

³⁴¹ A. S. Burrows, *Remedies for Torts and Breach of Contract* (3rd edn, Oxford, 2004), 141, citing *Schering Agrochemicals Ltd v. Resibel NV SA* (Court of Appeal, 26 November 1992, unreported, Court of Appeal transcript No. 1298 of 1992): on which see 18.59 at (2).

³⁴² A. S. Burrows, *Remedies for Torts and Breach of Contract* (3rd edn, Oxford, 2004), 143.

³⁴³ *Ibid.*

remain available in category (3) (concurrent contractual and tortious duties to take care), but it should be extended to category (2) (stand-alone contractual duty to take care). In short, this defence should apply whenever the defendant has breached a contractual obligation to exercise reasonable care, as distinct from a strict obligation.

6. RESTITUTIONARY CLAIMS³⁴⁴

- 18.51** Restitutionary claims are based on the defendant's unjust enrichment. The claim is not for the claimant's loss, but for the defendant's enrichment at the claimant's expense. Most restitutionary remedies arise independently of breach. However, breach of contract is an essential element in one restitutionary remedy, namely, the remedy of 'equitable account' (see the *Attorney-General v. Blake* line of cases at 18.56 ff below). The relevant enrichment can be money or services or goods. This cause of action can take various forms: it might be that the benefit was conferred as a result of the claimant's mistake of fact or law; or that there was a (total) failure of consideration, or duress, or undue influence, or abuse of fiduciary relationship,³⁴⁵ or an unjustified tax demand.
- 18.52** There are three main forms of restitutionary relief relevant to contract law: (1) money recovered for a total failure of consideration (on express recovery of payment clauses, see 17.04); (2) recovery in respect of goods or services; and (3) disgorgement of gains made in breach of contract. These will be explained in turn.
- 18.53** *Money recovered for a total failure of consideration.* A payor is entitled to recover money where there has been a 'total failure of consideration'.³⁴⁶ The *Fibrosa* case (1942)³⁴⁷ provides an example (which must suffice, for reasons of space):³⁴⁸

344 T. Baloch, *Unjust Enrichment and Contract* (Oxford, 2009); A. S. Burrows, *The Law of Restitution* (2nd edn, London, 2002); R. Goff and G. H. Jones, *The Law of Restitution* (7th edn, London, 2007); G. Virgo, *The Principles of the Law of Restitution* (2nd edn, Oxford, 2006); A. S. Burrows, E. McKendrick and J. Edelman, *Cases and Materials on the Law of Restitution* (2nd edn, Oxford, 2007).

345 *Calvert v. William Hill Credit Ltd* [2008] EWCA Civ 1427; [2009] Ch 330, at [53]; *Parker and Mellows: The Modern Law of Trusts* (9th edn, London, 2008), 10-048 ff; J. Edelman, 'When Do Fiduciary Duties Arise?' (2010) 126 LQR 302.

346 For criticism, see P. B. H. Birks, in F. D. Rose (ed.), *Consensus ad Idem: Essays on the Law of Contract in Honour of Guenter Treitel* (London, 1996), chapter 9.

347 [1943] AC 32, HL.

348 Other leading cases include *Rowland v. Divall* [1923] 2 KB 500, CA; *Rover International Ltd v. Cannon Films Sales Ltd* [1989] 1 WLR 912; *Barber v. NWS Bank* [1996] 1 WLR 641, CA; *Pan Ocean Shipping v. Creditcorp ('The Trident Beauty')* [1994] 1 WLR 161, 164-5, HL; *Stocznia Gdanska SA v. Latvian Shipping Co.* [1998] 1 WLR 574, HL; for restitution of money under a void contract, see *Westdeutsche Landesbank Girozentrale v. Islington London Borough Council* [1996] AC 669, 683, HL; *Guinness Mahon & Co. Ltd v. Kensington & Chelsea Royal London Borough Council* [1999] QB 215, 234-40, CA, Robert Walker LJ (considered in *Hauesund Kommune v. Depfa ACS Bank* [2010] EWCA Civ 579, at [62] and [85]; noted by A. Briggs and J. Edelman, (2010) 126 LQR 501, 503); decisions allowing partial failure in special situations: *Goss v. Chilcott* [1996] AC 788, PC (approving the High Court of Australia's decision in *David Securities Pty Ltd v. Commonwealth of Australia* (1992) 109 ALR 57, High Court of Australia; *Baltic Shipping Co. v. Dillon ('The Mikhail Lermontov')* (1993) 176 CLR 344, High Court of Australia; *DO Ferguson & Associates v. Sohl* (1992) 62 BLR 95, CA.

The *Fibrosa* case concerned an agreement (subject to English law) for an English supplier to sell machinery to be delivered to a Polish port. The foreign buyer paid £1,000 in advance. The contract was frustrated (16.01 ff) because the (supervening) German occupation of Poland in 1939 rendered performance illegal (the contract then terminated by operation of law (16.21) in accordance with the rule that there can be no trading with the enemy: it had become, as a result of supervening events, illegal to perform (16.07)).

The House of Lords held that the prepayment should be repaid because the payor had not received any of the promised 'consideration', that is, none of the machinery had been delivered (overruling the decision in *Chandler v. Webster* (1904),³⁴⁹ where the Court of Appeal had fallaciously barred recovery of payments whenever the payee had made to the payor a promise of performance; as the House of Lords noted in *Fibrosa*, although 'consideration' relevant to the formation of contracts (5.01 ff) can consist in the making of a promise, what counts in the context of the restitutionary claim for 'failure of consideration' is not the promise but actual performance of that promise). Furthermore, the House of Lords in the *Fibrosa* case held that, in this transaction, the relevant performance was delivery of machinery, and that preparation for its delivery did not count. For this reason, non-delivery involved total failure of performance.

18.54 In the context of frustrated contracts, however, recovery of money is now subject to the Law Reform (Frustrated Contracts) Act 1943 (16.22). The 1943 Act is confined to frustrated contracts. In that (narrow) category, section 1(2) of the Act allows money to be recovered even in the absence of a 'total failure'. But such recovery under the 1943 Act is subject to adjustment between the parties.³⁵⁰ Apart from frustrated contracts, where this Act applies, the common law claim for repayment based on 'total failure' (see the preceding paragraph) still applies to various other contexts.

18.55 *Recovery in respect of goods or services.* This is illustrated by the *British Steel* case (1984) (2.04)³⁵¹ (and by the *Whittle* case (2009),³⁵² discussed at 4.21 and by the *Wigan AFC* case discussed at 5.27). In the *British Steel* case (1984), Goff J held that there had been no true agreement because negotiations had not resolved the issue of potential liability for late delivery of building materials to the defendant's order. The question of restitutionary relief arose because British Steel had supplied steel to the defendant company, which had used it in its building project. It was plainly just that the building company should pay a fair market sum to the claimant. This award was based on restitutionary or unjust enrichment principles. The *British Steel* case concerned goods, but a similar award is available in the case of services performed to the order of the defendant, even though there is no agreement

349 [1904] 1 KB 493, CA.

350 Section 1(2) of the Law Reform (Frustrated Contracts) Act 1943.

351 *British Steel Corporation v. Cleveland Bridge* [1984] 1 All ER 504, Goff J.

352 *Whittle Movers Ltd v. Hollywood Express Ltd* [2009] EWCA Civ 1189; [2009] CLC 771, Waller, Dyson and Lloyd LJ; noted by P. S. Davies, (2010) 126 LQR 175–9.

or no valid contract.³⁵³ Here, a restitutionary sum of recompense, conferring a reasonable sum, can be awarded (known as a *quantum meruit*) for the performing party's benefit, as in *Planché v. Colburn* (1831) (recompense for work done in composing material no longer required by the defendant publisher),³⁵⁴ *Craven-Ellis v. Canons Ltd* (1936) (services performed under void contract),³⁵⁵ *William Lacey v. Davis* (1957) (work carried out in anticipation of contract; risk of abortive negotiations with defendant: see 12.04)³⁵⁶ and *Benedetti v. Sawiris* (award of an enhanced payment, exceeding the normal 'market value', to reflect figures used in negotiations subsequent to the actual performance of the work).³⁵⁷

- 18.56 *Disgorgement of gains made in breach of contract.* The House of Lords decision in *Attorney-General v. Blake* (2001) expands this category of restitutionary claim.³⁵⁸ Until the *Blake* case, the English courts had confined the remedy of 'account of profits' to two categories of breach of contract: (1) breach of contract also involving a breach of fiduciary duty (for example, breaches of contract by agents or solicitors);³⁵⁹ and (2) breach of property rights, as in the case of restrictive covenants agreed between freeholders (that is, an undertaking by A, a landowner, to B, another landowner, that A will refrain from certain activities, such as using the property for business purposes rather than as a residence; as we shall see at 18.60, within category (2), awards of an 'account' can be rationalised as compensating for loss of an opportunity to bargain for a release fee, and hence as a species of compensatory damages). But, in *Attorney-General v. Blake* (2001), the House of Lords, breaking free from these constraints, introduced the remedy of an account of profits for a simple breach of contract, without the need to show either a breach of a fiduciary duty or an infringement of a proprietary right. A clear illustration of the narrowness of these pre-*Blake* categories was *Surrey County Council v. Bredero Homes* (1993).³⁶⁰

353 A. S. Burrows, *The Law of Restitution* (2nd edn, London, 2002), 372–81; R. Goff and G. H. Jones, *The Law of Restitution* (7th edn, London, 2007), 26–008 ff; *MSM Consulting Ltd v. United Republic of Tanzania* [2009] EWHC 121 (QB), at [171], per Clarke J (distilling principles, with the assistance of Nicholas Strauss QC's decision in *Countrywide Communications Ltd v. ICL Pathway Ltd* [2000] CLC 324, 349: noted by P. Jaffey, [2000] *Restitution Law Review* 270–5).

354 (1831) 8 Bing 14.

355 [1936] 2 KB 403, CA.

356 [1957] 1 WLR 932, Barry J (see 12.04).

357 [2009] EWHC 1330, Patten J, especially at [571] (critically noted by A. Lodder, (2010) 126 LQR 42–7).

358 [2001] 1 AC 268 HL; J. Edelman, *Gain-Based Damages* (Oxford, 2002), chapter 5; E. McKendrick in A. S. Burrows and E. Peel (eds.), *Commercial Remedies: Current Issues and Problems* (Oxford, 2003), 93–119; A. S. Burrows, *Remedies for Torts and Breach of Contract* (3rd edn, Oxford, 2004), 395–407; J. Beatson, (2002) 118 LQR 377; R. Goff and G. H. Jones, *The Law of Restitution* (7th edn, London, 2007), 20–024 ff; and D. Howarth, in S. Hedley and M. Halliwell (eds.), *The Law of Restitution* (London, 2002), 11.7 to 11.31; A. S. Burrows, 'Are "Damages on the Wrotham Park Basis" Compensatory, Restitutionary or Neither?', S. Waddams, 'Gains Derived from Breach of Contract: Historical and Conceptual Perspectives', and R. Cunnington, 'The Measure and Availability of Gains-Based Damages for Breach of Contract', all three in D. Saidov and R. Cunnington (eds.), *Contract Damages: Domestic and International Perspectives* (Oxford, 2008), chapters 7–9, respectively; R. Cunnington, 'The Assessment of Gains-Based Damages for Breach of Contract' (2008) 71 MLR 559–86.

359 *Calvert v. William Hill Credit Ltd* [2008] EWCA Civ 1427; [2009] Ch 330, at [53]; *Parker and Mellows: The Modern Law of Trusts* (9th edn, London, 2008), 10–048 ff; J. Edelman, 'When Do Fiduciary Duties Arise?' (2010) 126 LQR 302.

360 *Surrey County Council v. Bredero Homes Ltd* [1993] 1 WLR 1361, CA.

In *Surrey County Council v. Bredero Homes* (1993), a local authority sold land to a developer and obtained a 'personal' covenant [not on these facts a restrictive covenant, which would have had a proprietary basis] that the developer would construct a specified number of houses, consistent with the initial planning permission. The covenant was to enable the authority to share in the planning gain if, as happened, planning permission was subsequently granted for the erection of more houses. In breach of covenant, the developer completed the development in accordance with a later planning permission. The defendant's decision to build more houses had not caused any financial loss to the local authority, but it had given the developer a large gain. The Court of Appeal agreed with the trial judge that, if the breach of contract did not also involve breach of a fiduciary duty or infringement of the claimant's property rights (see earlier in this paragraph), the authority should receive only nominal damages of £2. The court was not asked to consider the 'user principle' form of damages (18.59, 18.60) because the plaintiff had deliberately elected not to seek an injunction to prevent the development. And so the case was argued as an opportunity – rejected by the Court of Appeal – to award pure profit-stripping relief in the form of 'damages'.

In his note in the *Law Quarterly Review* on this case, Peter Birks (a great enthusiast for the expansion and conceptual ordering of unjust enrichment principles) vehemently condemned this restriction as a blot on English law.³⁶¹ As a result, judicial minds opened to the possibility of crafting an exceptional remedy of an account of profits, even in the absence of these two factors. As we shall see in the next paragraph, *Attorney-General v. Blake* (2001) has rendered an account of profits available in exceptional situations for a mere breach of contract without the need to pigeonhole the facts within either category (1) or category (2), as just set out. (Solène Rowan has also contended that the courts will uphold a clause stipulating that profit-disgorgement should be available to the innocent party, although she notes Burrows' doubt whether this will be appropriate in all commercial contexts.)³⁶²

- 18.57** The House of Lords in *Attorney-General v. Blake* (2001) introduced the remedy of an account of profits for a simple breach of contract, without the need to satisfy either breach of fiduciary duty or infringement of a proprietary right. Lord Nicholls (who gave the main speech)³⁶³ said that this remedy of an account should be treated as quite exceptional, and that it should be granted only if all four of the following (mostly opaque) criteria are satisfied: first, the claimant can show a legitimate interest; secondly, all other remedies are inadequate; thirdly,

361 P. B. H. Birks, (1993) 109 LQR 518, 520–1.

362 S. Rowan, 'For the Recognition of Remedial Terms Agreed Inter Partes' (2010) 126 LQR 448, 457–60, and noting the more cautious comments in A. S. Burrows, *The Law of Restitution* (2nd edn, London, 2002), 445.

363 [2001] 1 AC 268, HL.

the court in its discretion regards this as an appropriate response to the breach; and, fourthly, the gain is attributable to that breach. He said:³⁶⁴

An account of profits will be appropriate only in exceptional circumstances. Normally the remedies of damages, specific performance and injunction, coupled with the characterisation of some contractual obligations as fiduciary,³⁶⁵ will provide an adequate response to a breach of contract. It will be only in exceptional cases, where those remedies are inadequate, that any question of accounting for profits will arise. No fixed rules can be prescribed. The court will have regard to all the circumstances, including the subject matter of the contract, the purpose of the contractual provision which has been breached, the circumstances in which the breach occurred, the consequences of the breach and the circumstances in which relief is being sought. A useful general guide, although not exhaustive, is whether the plaintiff had a legitimate interest in preventing the defendant's profit-making activity and, hence, in depriving him of his profit.

The extraordinary facts of the *Blake* case (2001)³⁶⁶ seemed to four members of the House of Lords, including Lord Nicholls, to demand that English law should make this change (but, perhaps wisely, not even these facts could seduce the fifth and dissenting judge, Lord Hobhouse, into abandoning the restrictive approach explained at 18.56).

Blake, having been convicted in the 1960s of espionage,³⁶⁷ had been imprisoned in England. But he escaped to Moscow where he eventually published his memoirs. The UK government wanted to prevent the spy's London publisher from sending a second royalty cheque to the author in Russia. The House of Lords held that an 'equitable account' can be awarded against a party in breach in order to 'strip' him of a profit made at the claimant's expense, that is, as a result of a breach of contract. An injunction was granted to compel the publisher to pay the royalty sum to the Crown, Blake's employer before he had been dismissed for treachery. (In fact Brian Simpson³⁶⁸ contends that there was no contractual provision; and Sir Richard Buxton,³⁶⁹ in a journal article, has shown that the 'equitable account' argument, a point only considered by the House of Lords, in fact rendered this decision highly problematic.)

Cases decided since the *Blake* case will now be examined (these cases are summarised by Arden LJ in *Devenish Nutrition Ltd v. Sanofi-Anetis SA* (2008),³⁷⁰ a decision noted below at 18.61).

364 *Ibid.*, at 285.

365 *Calvert v. William Hill Credit Ltd* [2008] EWCA Civ 1427; [2009] Ch 330, at [53]; *Parker and Mellows: The Modern Law of Trusts* (9th edn, London, 2008), 10-048 ff; J. Edelman, 'When Do Fiduciary Duties Arise?' (2010) 126 LQR 302.

366 [2001] 1 AC 268, HL.

367 For a very detailed examination of the background facts, see A. W. B. Simpson, 'A Decision Per Incuriam' (2009) 125 LQR 433.

368 *Ibid.*, at 436-887, suggests that Blake did not have a contract of employment and had not 'signed' the Official Secrets Act in any contractual sense.

369 R. Buxton, 'How the Common Law Gets Made ...' (2009) 125 LQR 60, 73 ff.

370 [2008] EWCA Civ 1086; [2009] Ch 390, at [40] and [62] to [70]; noted by D. Sheehan, (2009) 125 LQR 222; C. Rotherham, 'Gains-Based Relief after AG v. Blake' (2010) 126 LQR 102-30; see also *Vercoe v.*

- 18.58 In the wake of *Blake* (18.56), Morritt V-C in *Esso Petroleum Ltd v. Niad Ltd* (2001) refused to strike out a claim (that is, a pre-trial application to dismiss a claim on the basis that it is legally doomed to fail, even if the pleaded facts are true) for an account of profits made by a petrol retailer in breach of the supplier's contractual requirement that retailers should reduce pump prices to match local competitors' prices. The decision to allow this claim to proceed in this commercial context is unconvincing. However, because this is a first instance decision on a pre-trial application for striking out, and not a final decision on the merits at trial,³⁷¹ the decision has little, if any, binding effect.
- 18.59 *Compensation for 'loss of opportunity to grant release of rights'*. The Court of Appeal's decision in *Experience Hendrix LLC v. PPX Enterprises Inc.* (2005),³⁷² made after the *Blake* case (see 18.57), demonstrates the exceptional nature of a full-blown account of profits. In this case, the Court of Appeal chose to award the claimant a less generous type of measure.

The estate of Jimi Hendrix (a rock guitarist) sued in respect of a settlement agreement which it had agreed with PPX. The latter had used master tapes in breach of that settlement. The Court of Appeal held that damages representing a reasonable price for their use should be awarded. The Court of Appeal refused to award a full account of the defendant's profits gained as a result of this breach. Mance LJ noted that there was nothing 'akin to a fiduciary relationship'.³⁷³ He contrasted the present case with the facts of the *Blake* case, where the former employee had signed a lifetime undertaking not to reveal official secrets (see 18.57). And so the Court of Appeal in the *Hendrix* case instead awarded a sum to reflect 'loss of opportunity to bargain for release or relaxation of the relevant rights'. This concept is known as 'the user principle': see 18.60 on its modern source, the *Wrotham Park* case (1974). The essential idea is that the court awards the victim a sum designed to simulate a notional release or relaxation fee which might have been paid by the defendant if he had courteously sought permission to make 'use' of the claimant's protected interest (as mentioned, this idea was not employed on the facts of the *Surrey County Council* case (1993),³⁷⁴ summarised at 18.56).

Damages for loss of opportunity to bargain were also awarded in *Lane v. O'Brien Homes Ltd* (2004). In this case, an extra house had been built, in breach of an agreement. The builder's profit from this breach was £280,000. But the judge merely awarded damages of £150,000 for loss of opportunity to bargain.³⁷⁵

Rutland Fund Management [2010] EWHC 424 (Ch), Sales J; noted by P. Devonshire, (2010) 126 LQR 526–9.

371 *The Times*, 19 April 2003, Morritt V-C.

372 [2003] EWCA Civ 323; [2003] 1 All ER (Comm) 830, CA.

373 *Calvert v. William Hill Credit Ltd* [2008] EWCA Civ 1427; [2009] Ch 330, at [53]; *Parker and Mellows: The Modern Law of Trusts* (9th edn, London, 2008), 10-048 ff; J. Edelman, 'When Do Fiduciary Duties Arise?' (2010) 126 LQR 302.

374 *Surrey County Council v. Bredero Homes Ltd* [1993] 1 WLR 1361, CA.

375 [2004] EWHC 303 (QB).

18.60 *Earlier consideration of the 'user principle'*. Brightman J's decision in *Wrotham Park Estate Co. v. Parkside Homes* (1974) is the modern starting point for the 'user principle'.³⁷⁶ In breach of a restrictive covenant, the defendant had built some houses on its land. In an action for damages *in lieu* of an injunction (which would have required demolition of these dwellings), Brightman J chose not to award the innocent party the whole of the gain made from this breach. Instead, he awarded the claimant a rather modest percentage of the defendant's profit. Commenting on the *Wrotham Park* case (1974), Lord Nicholls said in the *Blake* case (2001):

The existence of the new houses [in the 1974 case] did not diminish the value of the benefited land by one farthing. The judge considered that if the plaintiffs were given a nominal sum, or no sum, justice would manifestly not have been done. He assessed the damages at 5 per cent of the developer's anticipated profit, this being the amount of money which could reasonably have been demanded for a relaxation of the covenant.

It is clear that the award in the *Wrotham Park* case was not a full-blown 'account' of profits, but a quite different award designed to remedy loss of a bargaining opportunity: in this case, possible negotiation for a fee to be paid in return for relaxing the claimant's restrictive covenant. Curiously, Lord Nicholls in the *Blake* case treated the *Wrotham Park* case as the 'main plank' for his new approach, extolling it as a decision which 'still shines, rather as a solitary beacon, showing that in contract as well as tort damages are not always narrowly confined to recoupment of economic loss'.³⁷⁷ For Lord Nicholls, the case involved contractual relief aimed at depriving the defendant of a gain.³⁷⁸ However, the better view, as Lord Hobhouse in the *Blake* case (2001) insisted, is that the award in the *Wrotham Park* case was compensatory, the award of damages for loss arising from breach:

What has happened in such cases is that there has either actually or in effect been a compulsory purchase of the plaintiff's right of refusal. (The award of damages in tort for the conversion or detinue of goods is also an example of compulsory purchase as is demonstrated by the common law rule that the payment of the damages vests the title in the goods in the defendant.) What the plaintiff has lost is the sum which he could have exacted from the defendant as the price of his consent to the development. This is an example of compensatory damages. They are damages for breach. They do not involve any concept of restitution and so to describe them is an error.³⁷⁹

In the next paragraph, we shall consider the juridical nature of the 'user principle': is it truly 'compensatory' or 'restitutionary'?

³⁷⁶ [1974] 1 WLR 798, Brightman J.

³⁷⁷ *Blake* case, [2001] 1 AC 268, 282–3, HL.

³⁷⁸ *Ibid.*, at 283–4.

³⁷⁹ *Ibid.*, at 298 (see also *Veroe v. Rutland Fund Management* [2010] EWHC 424 (Ch), Sales J; noted by P. Devonshire, (2010) 126 LQR 526–9).

- 18.61 Further discussion of the ‘user principle’ occurred in the *WWF* case (2007).³⁸⁰ The claim was for compensatory damages for loss of the opportunity to exact a fee for release or modification of contractual rights, that is, in accordance with the ‘user principle’ (on which see 18.59).

The complaint was that defendant, the World Wrestling Federation, had breached an agreement controlling its use of the abbreviation ‘WWF’. The claimant also used those three letters, styling itself ‘The World Wide Fund’. In the first action, heard by Jacob J,³⁸¹ a claim for a (*Blake*-style) account of profits had failed. In the second stage of the litigation, a new claim on the same facts was made, based this time on the so-called ‘user principle’. The Court of Appeal’s decision in this second action was that the claimants were attempting to litigate a claim which should have been pleaded in the first litigation, and this was contrary to procedural principle, because it would involve giving the claimant a second bite at the cherry: ‘the claim to *Wrotham Park* damages (if it were to be raised at all) should have been raised before Mr Justice Jacob [in the earlier case] in conjunction with the claim to an account of profits.’³⁸²

The procedural aspect of the *WWF* appeal is sound. Claims arising on the same facts against the same alleged wrongdoer should be brought in the same action, rather than inefficiently in a series. This general procedural doctrine is known as ‘the rule in *Henderson v. Henderson*’, a rule clearly based on the principle of finality. In this 1843 decision, Wigram V-C said:³⁸³ ‘The plea of *res judicata*’³⁸⁴ applies, except in special cases, not only to points upon which the Court was actually required by the parties to form an opinion and pronounce a judgment, but to every point which properly belonged to the subject of litigation, and which the parties, exercising reasonable diligence, might have brought forward at the time.’ And so a claim for (1) an account of profits should be combined in a single action with (2) a claim for ‘user principle’ damages. Failure to plead (2) in the earlier litigation precludes the bringing of (2) in a second action.

However, the Court of Appeal took an unnecessary step and declared that, in essence, an account of profits is no less ‘compensatory’ than a claim on the ‘user principle’. According to this (mistaken) view, they are remedial twins and not merely siblings. Chadwick LJ said:³⁸⁵

To label [1] an award of damages on the *Wrotham Park* basis as a ‘compensatory’ remedy and [2] an order for an account of profits as a ‘gains-based’ remedy does not

380 *WWF–World Wide Fund for Nature v. World Wrestling Federation Entertainment Inc.* (‘No. 2’) [2007] EWCA Civ 286; [2008] 1 WLR 445, noted by R. Cunnington, [2007] CLJ 507.

381 *WWF* case (‘No. 1’) [2002] FSR 32, Jacob J; upheld in [2002] EWCA Civ 196; [2002] FSR 530.

382 *WWF* case (‘No. 2’) [2007] EWCA Civ 286; [2008] 1 WLR 445, at [74].

383 *Henderson v. Henderson* (1843) 3 Hare 100, 114, Wigram V-C; a modern discussion is in *Johnson v. Gore Wood & Co.* [2000] UKHL 65; [2002] 1 AC 1, 23B–D.

384 ‘*Res judicata*’ refers to a ‘matter having been decided’: N. Andrews, *The Modern Civil Process* (Tübingen, 2008), 8.22 to 8.27; G. Spencer Bower, A. K. Turner and K. R. Handley, *The Doctrine of Res Judicata* (3rd edn, London, 1996).

385 *WWF* case (‘No. 2’) [2007] EWCA Civ 286; [2008] 1 WLR 445, at [59]. Numbering added.

assist an understanding of the principles on which the court acts. [3] The two remedies should, I think, each be seen as a flexible response to the need to compensate the claimant for the wrong which has been done to him.

The first proposition (at (1) above) within this quotation is attractive: that the ‘user principle’ is compensatory. Such damages compensate the claimant for loss of the chance to bargain for release or at least relaxation of a right (whether the right released etc. is a property right, as in the *Wrotham Park* case (18.59), or a bare contractual one, as in the *Experience Hendrix* case (18.58)). It is not the aim of such a ‘loss of bargaining opportunity’ award to erase the defendant’s nefarious gain, but instead to compensate the claimant for his lost bargaining advantage. The law strives to put a monetary value on that lost opportunity. That value is not necessarily the amount of the gain made by the defendant in breaching the relevant right. (Admittedly, this question remains the subject of academic disputation: the view that *Wrotham Park* damages are compensatory is opposed by Burrows, who contends that the notional bargain is a mere fiction;³⁸⁶ but this allegation of fiction is flatly denied by Waddams.)³⁸⁷ However, propositions (2) and (3) of the quotation from Chadwick LJ’s judgment, set out above, are *unacceptable*: it cannot be correct to regard an *account of profits* as ‘compensatory’ when that relief is intended to provide exceptional relief measured by the defendant’s gain *where the claimant has suffered no equivalent loss*. This was the predicament of the UK government in the *Blake* case (18.57) (although damages under the ‘user principle’ might, it can now be suggested, have justified the government intercepting at least some of Blake’s royalty payments before they were sent by his publisher to his Moscow address). In short, therefore, an account of profits is not compensatory unless it is confined to awarding the claimant his *loss of an opportunity to bargain for a release fee*. Unless so confined, the profit-stripping award is purely ‘restitutionary’ or wholly gains-based, in the sense that the claim is awarded irrespective of the claimant having suffered equivalent ‘loss’.

Finally, the Court of Appeal in *Devenish Nutrition Ltd v. Sanofi-Anetis SA* (2008) refused an account of profits in the context of a tort claim.³⁸⁸ The defendants had been found guilty of anti-competitive behaviour because they had conducted a worldwide cartel concerning the prices of vitamins. Certain purchasers now sought an account of

386 A. S. Burrows, in M. Andenas and D. Fairgrieve (eds.), *Tom Bingham and the Transformation of the Law: A Liber Amicorum* (Oxford, 2009), 594–8; and A. S. Burrows, ‘Are “Damages on the *Wrotham Park* Basis” Compensatory, Restitutionary or Neither?’, in D. Saidov and R. Cunnington (eds.), *Contract Damages: Domestic and International Perspectives* (Oxford, 2008), chapter 7.

387 S. Waddams, ‘Gains Derived from Breach of Contract: Historical and Conceptual Perspectives’, in D. Saidov and R. Cunnington (eds.), *Contract Damages: Domestic and International Perspectives* (Oxford, 2008), 200 ff (earlier R. J. Sharpe and S. Waddams, (1982) 2 OJLS 290; cf his remark at S. Waddams, *Dimensions of Private Law* (Cambridge, 2003), 109); other discussion and *dicta* on this vexed issue are conveniently collected at R. Cunnington, (2007) 123 LQR 48, including *Jaggard v. Sawyer* [1995] 1 WLR 269, 281–2, 291, CA, *per* Bingham MR, and Millett LJ, the latter rejecting Steyn LJ’s comment in *Surrey County Council v. Bredero Homes Ltd* [1983] 1 WLR 1361, 1369, CA, that the ‘compensatory’ theory involves a ‘fiction’; *Gafford v. Graham* (1998) 76 P & CR 18; see also R. Cunnington, ‘The Assessment of Gains-Based Damages for Breach of Contract’ (2008) 71 MLR 559–86.

388 [2008] EWCA Civ 1086; [2009] Ch 390.

(some of) this ill-gotten profit. Arden and Longmore LJ examined the *Blake* case (2001). Arden³⁸⁹ and Tuckey LJ were not prepared to award an account on these facts because earlier Court of Appeal authority³⁹⁰ (antedating the *Blake* case and not cited by the House of Lords in that landmark decision) directly precluded this in the case of ‘non-proprietary torts’. Longmore LJ’s ground of refusal³⁹¹ was that the present claim for an account was not ‘exceptional’ and this meant that one of the criteria established in the *Blake* case had not been satisfied.

7. DECLARATIONS

- 18.62** A declaration is a non-monetary and non-coercive remedy. It merely involves the court stating definitively the facts and legal result in an action. Sometimes, that is enough. Indeed, a declaration might be the only relief sought.³⁹² For example, in *Lock v. Bell* (1931), a vendor obtained a declaration that the deposit of £120 on the sale of a public house had been forfeited validly.³⁹³ And, in *Patten v. Burke Publishing Co. Ltd* (1991), a writer, now proposing to deal with publisher B, sought a declaration that he could safely do so because he was no longer contractually committed to write for publisher A.³⁹⁴ So-called ‘negative declarations’ (applications to gain a binding declaration that the claimant *is not legally liable to the other party*) are often sought in English civil proceedings as a tactic to preclude proceedings by a defendant against a claimant in another jurisdiction.³⁹⁵ Finally, it should be noted that, where no substantial loss has resulted, or substantial damages have not been claimed, an award of ‘nominal damages’ (on which see 18.23 at (2) above) is functionally equivalent to a declaration that ‘there has been a bare breach’.

8. ‘STAYS’ UPON LEGAL PROCEEDINGS

- 18.63** This is a decision by the court to place proceedings in suspense, until the ‘stay’ is lifted. A ‘stay’ is sometimes a contractual remedy, in the sense that it can be a judicial response to a breach of contract.

For example, in *Cable & Wireless plc v. IBM United Kingdom Ltd* (2002) (2.13), Colman J upheld an agreement by two commercial parties whereby: (1) they agreed to negotiate disputes; (2) they further agreed thereafter, if necessary, to conduct a mediated negotiation; and (3) an aggrieved party could, if necessary, finally resort to formal litigation. One party had jumped straight from stage (1) to stage (3). The judge held that failure by one party to proceed to stage (2) involved a breach. The ‘remedy’ was to issue a stay of

389 *Ibid.*, at [76] and [156].

390 *Stoke-on-Trent City Council v. Wass* [1998] 1 WLR 1406, CA.

391 [2008] EWCA Civ 1086; [2009] Ch 390, at [147] to [149].

392 Zamir and Woolf, *The Declaratory Judgment* (3rd edn, London, 2001).

393 [1931] 1 Ch 35, Maugham J.

394 [1991] 1 WLR 541.

395 Dicey, *Morris and Collins, The Conflict of Laws* (14th edn, London, 2006), 12-039 ff.

the High Court proceedings brought at stage (3), prematurely on these facts, in breach of the dispute-resolution agreement.³⁹⁶

As mentioned at 7.33, Ormrod J in *Snelling v. John Snelling Ltd* (1973)³⁹⁷ issued a stay of the action before him in order to give effect to a contract intended to protect a third party against action.

9. INTEREST ON MONEY CLAIMS

18.64 Interest is available for money claims, whether the claim is for non-payment of a debt (18.03 ff), compensatory damages (18.23 ff) or a pecuniary award in the law of restitution (18.51 ff). At present,³⁹⁸ the law is as follows:

- (1) The court, ‘when giving judgment on the principal sum’, has a statutory power to award *simple* interest in an action for damages or non-payment of a debt (section 35A of the Senior Courts Act 1981).
- (2) Section 35A of the Senior Courts Act 1981 extends to the situation where the principal sum was (fully) paid only after commencement of formal proceedings but before judgment was obtained.
- (3) Also under statute, interest can be compensated by a claim for statutory interest in respect of a late payment of a debt, even where no proceedings were commenced with respect to the principal sum. The Late Payment of Commercial Debts (Interest) Act 1998 (as amended)³⁹⁹ confers a right to *simple* interest (at a specified level) on the unpaid price of goods or services *if the supplier and recipient are both acting in the course of business* (section 2); the interest becomes payable as from: (a) any agreed date of payment (section 4(3)); (b) thirty days after the supplier’s performance or notice to the purchaser of the amount of the debt or of the quantified debt claim (section 4(5)); or, where that amount is unascertained, the date when the purchaser has notice of the amount claimed as the debt.
- (4) At common law, the House of Lords in *Sempre Metals Ltd v. Inland Revenue Commissioners* (2007)⁴⁰⁰ held that *simple and compound* interest can be awarded by English courts for breaches of contract or tort, for non-payment of a debt, or in respect of restitutionary claims. This decision (a) rejects a long line of problematic

³⁹⁶ [2002] 2 All ER (Comm) 1041.

³⁹⁷ [1973] QB 87, Ormrod J.

³⁹⁸ A draft Civil Law Reform Bill, clauses 10–14, now withdrawn, contained a proposed consolidation of the law governing pre-judgment and post-judgment interest; and these draft provisions would empower the Lord Chancellor to make Orders authorising the award, in situations to be specified, of compound interest. Ministry of Justice, *Civil Law Reform Bill* (Consultation Paper No. 53/09, December 2009).

³⁹⁹ Late Payment of Commercial Debts Regulations 2002 (SI 2002 No. 1674).

⁴⁰⁰ [2007] UKHL 34; [2008] 1 AC 561, at [94] to [100], *per* Lord Nicholls; at [16], *per* Lord Hope; at [164] and [165], *per* Lord Walker; at [226], *per* Lord Mance; at [140], *per* Lord Scott; noted by G. Virgo, [2007] CLJ 510; C. Nicholl, (2008) 124 LQR 199; *McGregor on Damages* (18th edn, London, 2009), 15.060 ff; and, for fuller discussion, see P. Ridge, ‘Pre-Judgment Compound Interest’ (2010) 126 LQR 279–301; the *Sempre* case was considered in *Parabola Investments Ltd v. Browallia Cal Ltd* [2010] EWCA Civ 486 at [51] ff; see 9.13.

contrary authority (chronicled by Lord Nicholls);⁴⁰¹ and (b) renders otiose the Law Commission's proposals for change.⁴⁰² Lord Mance made this important observation in the *Sempra* case:⁴⁰³

The present case should not therefore be seen as a charter for claims, still less for claims on a compound basis, in respect of interest losses following a breach of contract, where there is no contractual stipulation for its recovery, simply because it can be said that the situation was one where loss of interest might foreseeably, and did in fact, follow on breach ... Before loss by way of interest is recoverable as damages, the higher threshold of reasonable contemplation must be crossed ... in the sense explained in '*The Heron II*' (1969) under either limb [of the *Hadley v. Baxendale* principle of remoteness: on those two cases, see 18.43 cases (1) and (2)] when the contract was made and is specifically pleaded and proved on that basis.

- (5) The Arbitration Act 1996 empowers arbitrators to order compound interest to be paid on sums declared payable in the arbitrator's 'award' (the arbitral equivalent of a court judgment).⁴⁰⁴

401 [2007] UKHL 34; [2008] 1 AC 561, at [74] ff (rejecting, notably, *Page v. Newman* (1829) 9 B & C 378 (King's Bench); *London, Chatham & Dover Railway Co. v. South Eastern Railway Co.* [1893] AC 429, HL; *President of India v. La Pintada Cia Navigation SA* [1985] AC 104, HL; *President of India v. Lips Maritime Corporation* [1988] AC 395, HL, survives, but is of minor significance: no common law damages for late payment of damages.

402 Law Commission, *Report on Pre-Judgment Interest on Debts and Damages* (Law Commission Report No. 287, London, 2004); earlier, Law Commission, *Compound Interest* (Law Commission Consultation Paper No. 167, London, 2002).

403 *Ibid.*, at [216].

404 Section 49(3) of the Arbitration Act 1996; Departmental Advisory Committee's *Report on the Arbitration Bill* (1996), at [235] to [238]: report reproduced in M. Mustill and S. Boyd, *Commercial Arbitration: Companion Volume* (London, 2001).

Chapter contents

1. Introduction *para.* 19.01
2. Liquidated damages and the penalty doctrine *para.* 19.02
3. Relief against forfeiture of money instalments *para.* 19.25
4. Deposits *para.* 19.27

19

Consensual remedies for breach of contract: liquidated damages and deposits

1. INTRODUCTION

19.01 Summary of main points

- (1) The parties can agree upon 'liquidated damages', that is, an amount of compensation payable in the event of breach of the contract, or one of its terms; or they can agree that a sum should be paid in advance as a deposit to induce a party to perform (see (7) below). These are the two main topics discussed in this chapter.
- (2) The 'penalty doctrine' invalidates a liquidated damages clause which stipulates that the party in breach shall pay a sum that is 'extravagant and unconscionable' in comparison with the greatest loss that could be contemplated at the time the contract was formed as likely to be suffered by breach of the relevant substantive term.
- (3) But the penalty doctrine only applies to sums payable upon breach and not where the sum is payable in other circumstances.
- (4) The courts have recently adopted the criterion whether a clause was intended to deter the other party from breaching the contract; but it will be submitted that this test is unnecessary and unhelpful; the better test is that stated at (2) above, the substantive criterion of an 'extravagant and unconscionable' mismatch between the amount stipulated as payable upon breach and the greatest loss which might be contemplated at the time the contract was formed.
- (5) The courts can invalidate, but are reluctant to do so, liquidated clauses contained in commercial agreements. Some commentators suggest that the court should go

further and abandon their penalty jurisdiction, and that the law would be confined to the Unfair Terms in Consumer Contracts Regulations 1999 (applicable only where the disadvantaged party is a consumer: 15.33). However, this contention is not the law and, as submitted here, should not be adopted.

- (6) *Stockloser v. Johnson* (1954)¹ suggests that sums payable under a contract by way of instalments (other than as a deposit, on which see below) cannot be validly retained by the innocent party if this would amount to a 'penal and unconscionable' forfeiture in the relevant case.
- (7) Deposits are sums paid to secure completion of the anticipated performance. A deposit is validly forfeited if the payor has defaulted in performance of the contract (unless the statutory or common law doctrine mentioned at (9)(a) and (b) below invalidates the deposit).
- (8) The amount of the deposit does not have to correspond with the likely loss: in other words, the 'penalty jurisdiction' (see (5) above) does not govern deposits. The innocent party is entitled to seek common law compensation in excess of the deposit, if such additional loss can be shown.
- (9) A deposit of 10 per cent for completion of a contract for the purchase of land, or the conclusion of a contract for the grant of a lease of real property, is now standard. Such a deposit will survive challenge under both (a) the statutory regime applicable to 'relief' against forfeiture of deposits and (b) the common law doctrine for relief against deposits 'unreasonable' in amount.

T. Downes, in P. B. H. Birks (ed.), *Wrongs and Remedies in the Twenty-First Century* (Oxford, 1996), chapter 11

M. Chen-Wishart, in P. B. H. Birks (ed.), *Wrongs and Remedies in the Twenty-First Century* (Oxford, 1996), chapter 12

L. Gullifer, in A. Burrows and E. Peel (eds.), *Commercial Remedies: Current Issues and Problems* (Oxford, 2003), 191

S. Rowan, 'For the Recognition of Remedial Terms Agreed Inter Partes' (2010) 126 LQR 448, 460 ff

Scottish Law Commission, *Penalty Clauses* (Scottish Law Commission Report No. 171, Edinburgh, 1999)

¹ [1954] 1 QB 476, CA.

2. LIQUIDATED DAMAGES AND THE PENALTY DOCTRINE²

19.02 *Attractions of the liquidated damages clause.* Liquidated damages clauses are attractive for many reasons: first, such a clause enables the parties at the moment of contractual formation to know the extent of their prospective liability; secondly, once breach has occurred, the clause relieves the claimant of the expense and uncertainty of proving loss;³ thirdly, it maintains fidelity to promises by acting as an incentive to performance; and, finally, it enables a party to stipulate for (non-punitive) protection beyond the technical limits of common law damages (see below). However, the ‘penalty doctrine’ prevents the innocent party stipulating for a flagrantly punitive, and hence non-compensatory, sum. The same doctrine also protects the guilty party from being coerced into soldiering on and avoiding the monetary sanction. Without this rule, well-advised parties could use money sanctions to induce individuals to perform personal services even if they no longer wished to do so. As mentioned at 18.17 and 18.22, specific performance or injunctions will not be granted where their *direct or indirect* effect would be to compel performance of such contracts.

19.03 *Fundamental statement of the penalty doctrine.* Dillon LJ noted in 1989: ‘There is no doubt that the [English penalty doctrine] originated in equity [1.25], and is of long standing.’⁴ As for this doctrine’s detailed rules, Lord Dunedin gave the seminal analysis in *Dunlop Pneumatic Tyre Co. Ltd v. New Garage and Motor Co. Ltd* (1915):⁵

1. Though the parties to a contract who use the words ‘penalty’ or ‘liquidated damages’ may *prima facie* be supposed to mean what they say, yet the expression used is not conclusive. The Court must find out whether the payment stipulated is in truth a penalty or liquidated damages ...

2. The essence of a penalty is a payment of money stipulated as *in terrorem* of the offending party; the essence of liquidated damages is a genuine covenanted pre-estimate of damage ...

3. The question whether a sum stipulated is a penalty or liquidated damages is a question of construction to be decided upon the terms and inherent circumstances of each

2 A. S. Burrows, *Remedies for Torts and Breach of Contract* (3rd edn, Oxford, 2004), 440–55, especially 449–51; G. H. Treitel, *Remedies for Breach of Contract: A Comparative Account* (Oxford, 1988), 208–34; L. Gullifer, in A. S. Burrows and E. Peel (eds.), *Commercial Remedies: Current Issues and Problems* (Oxford, 2003), 191; T. Downes, in P. B. H. Birks (ed.), *Wrongs and Remedies in the Twenty-First Century* (Oxford, 1996); M. Chen-Wishart, in P. B. H. Birks (ed.), *Wrongs and Remedies in the Twenty-First Century* (Oxford, 1996); S. Rowan, ‘For the Recognition of Remedial Terms Agreed Inter Partes’ (2010) 126 LQR 448, 460 ff; Scottish Law Commission, *Penalty Clauses* (Scottish Law Commission Report No. 171, Edinburgh, 1999); on the nineteenth-century history of this topic, see M. Lobban, in W. Cornish, J. S. Anderson, R. Cocks, M. Lobban, P. Polden and K. Smith, *The Oxford History of the Laws of England*, vol. XII, 1820–1914: *Private Law* (Oxford, 2010), 523 ff.

3 *Robophone Facilities Ltd v. Blank* [1966] 1 WLR 1428, 1447F, CA, per Diplock LJ.

4 *Jobson v. Johnson* [1989] 1 WLR 1026, 1032, CA, per Dillon LJ.

5 *Dunlop Pneumatic Tyre Co. Ltd v. New Garage and Motor Co. Ltd* [1915] AC 70, 86–8, HL, per Lord Dunedin.

particular contract, judged of as at the time of the making of the contract, not as at the time of the breach ...

4. To assist this task of construction various tests have been suggested, which if applicable to the case under consideration may prove helpful, or even conclusive. Such are:

- (a) *It will be held to be a penalty if the sum stipulated for is extravagant and unconscionable in amount in comparison with the greatest loss that could conceivably be proved to have followed from the breach.*
- (b) It will be held to be a penalty if the breach consists only in not paying a sum of money, and the sum stipulated is a sum greater than the sum which ought to have been paid ... This though one of the most ancient instances is truly a corollary to the last test ...
- (c) There is a presumption (but no more) that it is a penalty when 'a single lump sum is made payable by way of compensation, on the occurrence of one or more or all of several events, some of which may occasion serious and others but trifling damage'. On the other hand:
- (d) It is no obstacle to the sum stipulated being a genuine pre-estimate of damage, that the consequences of the breach are such as to make precise pre-estimation almost an impossibility. On the contrary, that is just the situation when it is probable that pre-estimated damage was the true bargain between the parties.

Point (d) is important: the courts must be alive to the difficulties faced when trying to make a precise prediction of the losses likely to flow from breach.⁶

19.04 In the *Alfred McAlpine* case (2005),⁷ Jackson J glossed the words in italic above in *Dunlop Pneumatic Tyre Co. Ltd v. New Garage and Motor Co. Ltd* (1915) (19.03). In his view, those words require 'a substantial discrepancy between the level of damages stipulated in the contract and the level of damages which is likely to be suffered'.

For example, in *CMC Group plc v. Michael Zhang* (2006),⁸ a settlement agreement between the parties provided that, if Z continued to make complaints of ill-treatment against CMC's employees, Z would have to pay a sum equivalent to the amount of the settlement (US\$40,000). The Court of Appeal held that this clause was a penalty because it bore no relation to the loss likely to flow from breach, and it had been inserted to deter breach of the settlement agreement rather than to quantify loss.

19.05 A liquidated damages clause can validly provide more generous compensation than that awarded by the courts. This *laissez-faire* approach to agreed 'compensation' seems

⁶ *Ibid.*, at 87–8.

⁷ *Alfred McAlpine Capital Projects Ltd v. Tilebox Ltd* [2005] EWHC (TCC) 281; [2005] BLR 271, 280, at [48], per Jackson J.

⁸ [2006] EWCA Civ 408.

sound, unless the clause aims to confer an ‘extravagant and unconscionable’ right to payment.⁹ For example, the parties can displace the rules governing remoteness (18.40),¹⁰ or mitigation (18.49)¹¹ (*query* the general rule denying recovery for ‘profits gained from breach’?).¹²

- 19.06** *Objective test.* In the *Alfred McAlpine* case (2005),¹³ Jackson J also noted that the test is objective. It ‘does not turn upon the genuineness or honesty of the party or parties who made the pre-estimate’ (furthermore, the parties’ own description of the relevant damages clause as ‘liquidated’ or ‘penalty’ is not decisive).¹⁴ The party arguing for invalidity of the damages clause has the burden of proof of showing that it is a penalty.¹⁵
- 19.07** *Assessment at date of formation and not of breach.* The penalty test is applied retrospectively by the court, with regard to the situation ‘as at the time of the making of the contract, not as at the time of the breach’¹⁶ (although the actual loss is a clue to ‘what could reasonably be expected to be the loss at the time the contract was made’).¹⁷
- 19.08** *Breach triggering liability.* The House of Lords affirmed in the *Export Credits Guarantee Department* case (1983) (19.09),¹⁸ and the Court of Appeal in the *Euro London Appointments* case (2006)¹⁹ confirmed, that a clause challenged on the basis that it was in fact a penalty

9 *Murray v. Leisureplay plc* [2005] EWCA 963; [2005] IRLR 946, CA; noting also the result in the *Dunlop Pneumatic* case, [1915] AC 70, HL.

10 *Robophone* case, [1966] 1 WLR 1428, 1447–9, CA, *per* Diplock LJ (clause proving enhanced recovery in respect of loss not covered by ‘limb 2’ of *Hadley v. Baxendale* (1854) 9 Exch 341; but, surprisingly, the Law Commission thought this unpersuasive: Law Commission, *Penalty Clauses and Forfeiture of Monies Paid* (Law Commission Consultation Paper No. 61, London, 1975), at [44]).

11 *Murray v. Leisureplay plc* [2005] EWCA 963; [2005] IRLR 946, CA (upholding a clause requiring the guilty party to pay a wrongfully dismissed party a year’s salary in the event of breach, without adjustment requiring the employee to mitigate his loss).

12 A. S. Burrows, *Remedies for Torts and Breach of Contract* (3rd edn, Oxford, 2004), 444–5 (considering development in *Attorney-General v. Blake* [2001] 1 AC 268, HL, 18.56).

13 *Alfred McAlpine Capital Projects Ltd v. Tilebox Ltd* [2005] EWHC (TCC) 281; [2005] BLR 271, 280, at [48], *per* Jackson J.

14 *Elphinstone v. Monkland Iron and Coal Co.* (1886) 11 App Cas 32; *Cellulose Acetate Silk Co. Ltd v. Widnes Foundry* (1925) Ltd [1933] AC 20, 25 HL; see also the *Duffen* case, at 19.15.

15 *Murray v. Leisureplay plc* [2005] EWCA 963; [2005] IRLR 946, CA, at [106], *per* Clarke LJ.

16 *Dunlop Pneumatic Tyre Co. Ltd v. New Garage and Motor Co. Ltd* [1915] AC 70, 87, HL, citing *Commissioner for Public Works v. Hills* [1906] AC 368, PC, and *Webster v. Bosanquet* [1912] AC 394, PC; Law Commission, *Penalty Clauses and Forfeiture of Monies Paid* (Law Commission Consultation Paper No. 61, London, 1975), at [30] and [41] (noting that the converse approach has gained favour in several other jurisdictions).

17 *Philips Hong Kong Ltd v. Attorney-General for Hong Kong* (1993) 61 BLR 41, 59, PC, *per* Lord Woolf; ‘date of formation’ principle not adopted in the USA, P. R. Kaplan, (1977) 50 *Southern California Law Review* 1055, 1072.

18 [1983] 1 WLR 399, HL (applied in *Jervis v. Harris* [1996] Ch 195, CA, and in the *Euro London* case: see 19.08); for earlier criticism, see *Bridge v. Campbell Discount* [1962] AC 600, 631, HL, *per* Lord Denning; Law Commission, *Penalty Clauses and Forfeiture of Monies Paid* (Law Commission Consultation Paper No. 61, London, 1975), Part III.

19 *Euro London Appointments Ltd v. Claessens International Ltd* [2006] EWCA Civ 385; [2006] 2 Lloyd’s Rep 436, at [29]; also supported by *Export Credits Guarantee Department v. Universal Oil Products Co.* [1983] 1 WLR 399, HL (19.09) (applied in *Jervis v. Harris* [1996] Ch 195, CA), both cited by Andrew Smith J in *Office of Fair Trading v. Abbey National plc* [2008] EWHC 875 (Comm), at [295] ff.

must concern a payment which is triggered by *breach*, that is, a *culpable failure to satisfy a contractual obligation*. If there is a different trigger, the relevant clause will not be a penalty.

In *Office of Fair Trading v. Abbey National plc* (2008)²⁰ (the bank charges litigation) (the main discussion of this case is at 15.36; the common law 'penalty' point under consideration here was not taken to the Court of Appeal²¹ nor to the Supreme Court), Andrew Smith J held²² that the penalty doctrine cannot apply to the banking practice (supported by written terms) of charging a fee for unauthorised loans granted by the bank when a customer exceeds his credit limit on his current account. In that situation, the customer does not commit a breach of his contract towards the bank. And so the fee cannot be regarded as a penalty at common law (for statutory regulation of such incidental banking fees under the Unfair Terms in Consumer Contracts Regulations 1999, see 15.33 ff).

- 19.09 *Need for breach as between payor and payee.* As the House of Lords further stated in the *Export Credits* case (1983),²³ the penalty doctrine can be invoked by the proposed *payor* only where the clause is triggered by *breach of an obligation owed by the payor to the payee*.

In *Export Credits Guarantee Department v. Universal Oil Products Co.* (1983), the Export Credits Guarantee Department (ECGD) agreed to guarantee payments by Universal Oil Products (UOP) to Kleinwort Benson, a bank. In the event of the ECGD becoming liable on those contracts of guarantee, UOP agreed to indemnify the ECGD. UOP argued that its liability to the ECGD was triggered by UOP's breach *vis-à-vis* Kleinwort Benson, and so the ECGD/UOP obligation might be vulnerable to attack as a penalty. But the defect in this argument was that English law required the breach to have been a primary obligation owed by the payor to the payee, that is, by UOP to the ECGD. In this case, there was no such primary obligation; instead, that primary obligation was owed by UOP to Kleinwort Benson.

As Lord Roskill (with whom the other members of the House of Lords agreed) said:²⁴

The clause was not a penalty clause because it provided for payment of money on the happening of a specified event other than a breach of contractual duty owed by the contemplated payer to the contemplated payee ... This is not a case where the ECGD are seeking to recover more than their actual loss as compensation by way of damages for breach of a contract to which they were

20 [2008] EWHC 875 (Comm); M. Chen-Wishart, (2008) 124 LQR 501–8; P. S. Davies, [2008] CLJ 466–9.

21 [2009] EWCA Civ 116; [2009] 2 WLR 1286, at [11]; M. Chen-Wishart, (2009) 125 LQR 389–93; but note Lord Phillips' *dictum* at [2009] UKSC 6; [2009] 3 WLR 1215, at [83], on which see C. Conte, (2010) 126 LQR 529, 531, also noting the (orthodox) decision on this point in *UK Housing Alliance (North West) Ltd v. Francis* [2010] EWCA Civ 117; [2010] 3 All ER 51).

22 [2008] EWHC 875 (Comm), at [295] to [323].

23 [1983] 1 WLR 399, HL (applied in *Jervis v. Harris* [1996] Ch 195, CA and in the *Euro London* case: see 19.08); for earlier criticism, see *Bridge v. Campbell Discount* [1962] AC 600, 631, HL, *per* Lord Denning; Law Commission, *Penalty Clauses and Forfeiture of Monies Paid* (Law Commission Consultation Paper No. 61, London, 1975), Part III.

24 [1983] 1 WLR 399, 401, 403, HL.

a party. They are seeking, and only seeking, to recover their actual loss, namely the sums which they became legally obliged to pay and have paid to Kleinworts ... I find it impossible to see how on the facts there can be any room for the invocation of the law relating to penalty clauses.

The *Export Credits* case was considered by Chadwick LJ in the *Euro London Appointments* case (2006).²⁵

- 19.10 *Types of clause covered by the penalty jurisdiction.* The penalty doctrine is not confined to clauses ('liquidated damages clauses') quantifying the amount of damages to be paid in the event of breach (although that will be the most common type of clause). In fact, four other types of clause are subject to this jurisdiction: (1) loss of a right to a refund, or loss of a right to a payment;²⁶ (2) loss of a right to a discount;²⁷ (3) clauses requiring the re-transfer of property in the event of the payor's default, where the value of the property to be handed back exceeds the amount of the monetary default;²⁸ (4) a 'debt' payable in the event of breach, for example, liability to pay a price if – in contravention of another obligation in the same contract – the buyer does not purchase a minimum quantity from the other party. As for (4), Burton J said in the *M & J Polymers* case (2008): 'It is clear that, for example, a minimum payment clause in a hire-purchase agreement can be held to be a penalty, even though expressed as a claim in debt.'²⁹ However, on the facts of that case, Burton J concluded that the relevant minimum payment clause was not a penalty and had instead been a fair provision inserted to achieve a sound commercial objective following free and open negotiations. He said:³⁰ 'The negotiations took place between extremely well qualified, able and savvy commercial men against a very significant commercial background, including a background of previous dealings.'
- 19.11 *Commercial parties.* Lord Woolf said in the *Philips Hong Kong* case (1993):³¹ '[T]he court has to be careful not to set too stringent a standard and to bear in mind that what the parties have agreed should normally be upheld. Any other approach will lead to undesirable uncertainty, especially in commercial contract.'³² Jackson J in the *Alfred McAlpine* case (2005) also noted that the courts are reluctant to upset liquidated damages clauses if they have been agreed between non-consumers.³³ He found only a handful of 'cases

25 *Euro London* case, [2006] EWCA Civ 385; [2006] 2 Lloyd's Rep 436, at [28].

26 *General Trading Company (Holdings) Ltd v. Richmond Corporation Ltd* [2008] EWHC 1479 (Comm); [2008] 2 Lloyd's Rep 475, at [113], *per* Beatson J (this point was *obiter*, see [109]; but the review of modern developments at [109] to [131] is helpful).

27 On (2) and (3), see the *Euro London* case, [2006] EWCA Civ 385; [2006] 2 Lloyd's Rep 436 (considered in the *M & J Polymers Ltd* case, [2008] EWHC 344 (Comm), at [42]).

28 *Jobson v. Johnson* [1989] 1 WLR 1026, CA.

29 *M & J Polymers Ltd v. Imerys Minerals Ltd* [2008] EWHC 344 (Comm); [2008] 1 Lloyd's Rep 541, at [41], *per* Burton J.

30 *Ibid.*, at [40] to [48], especially at [46].

31 *Philips Hong Kong Ltd v. Attorney-General for Hong Kong* (1993) 61 BLR 41, 54–5, 59, PC; *Robophone Facilities Ltd v. Blank* [1966] 1 WLR 1428, 1447, CA, *per* Diplock LJ.

32 *Philips Hong Kong Ltd v. Attorney-General for Hong Kong* (1993) 61 BLR 41, 61.

33 *Alfred McAlpine Capital Projects Ltd v. Tilebox Ltd* [2005] EWHC (TCC) 281; [2005] BLR 271, 280, at [48], *per* Jackson J.

where the relevant clause has been struck down as a penalty',³⁴ and these were, in his word, situations where 'there was a very wide gulf between (a) the level of damages likely to be suffered, and (b) the level of damages stipulated in the contract'.

- 19.12 *Equality of bargaining power.* Nevertheless, as the Court of Appeal's decision in the *Jeancharm* case (2003) shows, even between commercial parties of roughly equal bargaining strength, an intrinsically 'extravagant and unconscionable' clause (on the facts, one which required payment of interest on a commercial debt of 260 per cent a year) will be struck down.³⁵ However, Jacob LJ said in the *Jeancharm* case: '[O]ne should be careful before deciding whether or not a clause is a penalty when the parties are of equal bargaining power'.³⁶
- 19.13 *Muddying the waters: the suggested test of 'no deterrent purpose'.* The Court of Appeal in the *Murray* case (2007) said that the real issue is whether the innocent party's main purpose was to insert a payment clause containing a sum *so large that it would deter the other from breaching*, rather than to provide compensation.³⁷ The court said that there should be no automatic conclusion that a non-compensatory element renders the clause 'deterrent' in aim and hence invalidates the clause. Otherwise, Buxton LJ said, the approach would become unacceptably 'rigid and inflexible'.³⁸ Burton J followed this approach in the *M & J Polymers* case (2008).³⁹
- 19.14 The criterion of a 'deterrent purpose' is a controversial change of emphasis. The test in the seminal *Dunlop* case (19.03) refers to an 'extravagant and oppressive' difference between 'the greatest possible loss' and the amount stipulated for. This is an objective test, pitched in favour of the payee, and, it is submitted, this approach is sound. There is no need to obscure matters by referring to the payee's intention in procuring the relevant clause: after all, no real monetary threat can be made unless the stipulated sum greatly exceeds the ordinary common law measure of compensation. For this reason, the search for a *deterrent purpose* is unhelpful, as Lord Radcliffe noted in *Bridge v. Campbell Discount* (1962).⁴⁰
- 34 Citing *Commissioner of Public Works v. Hills* [1906] AC 368, PC, *Bridge v. Campbell Discount Co. Ltd* [1962] AC 600, HL, *Workers Trust and Merchant Bank Ltd v. Dojap Investments Ltd* [1993] AC 573, PC (arguably a case on common law relief against excessive deposits: see 19.35) and *Ariston SRL v. Charly Records* (Court of Appeal, 13 March 1990); see also *CMC Group plc v. Michael Zhang* [2006] EWCA Civ 408; *Jobson v. Johnson* [1989] 1 WLR 1026, CA; *Duffen v. FRA BO SpA, The Times*, 15 June 1998, CA; *Jeancharm Ltd v. Barnet Football Club Ltd* [2003] EWCA Civ 58, 92 Con LR 26.
- 35 *Jeancharm Ltd v. Barnet Football Club Ltd* [2003] EWCA Civ 58; 92 Con LR 26.
- 36 *Ibid.*, at [15].
- 37 *Murray v. Leisureplay plc* [2005] EWCA 963; [2005] IRLR 946, at [110] to [118], especially at [106], *per* Clarke and Buxton LJ (noting *Cines Bes Filmclik ve Yapincilik AS v. United International Pictures* [2003] EWCA Civ 1669, at [13], *per* Mance LJ, and *Lordsvale Finance plc v. Bank of Zambia* [1996] QB 752, 762G, Colman J).
- 38 *Murray v. Leisureplay plc* [2005] EWCA 963; [2005] IRLR 946, at [42].
- 39 [2008] EWHC 344 (Comm); [2008] 1 Lloyd's Rep 541, at [40] to [48], especially at [46]; and *General Trading Company (Holdings) Ltd v. Richmond Corporation Ltd* [2008] EWHC 1479 (Comm); [2008] 2 Lloyd's Rep 475, at [109] ff, *per* Beatson J (an *obiter* discussion, but a helpful review of modern developments).
- 40 [1962] AC 600, 621–2, HL.

Furthermore, the quest for a *deterrent purpose* would complicate matters because it would require the court to determine what the common intention of the parties was, who inserted the relevant clause, and what the purpose of its insertion was. To avoid these difficulties, it is submitted that the law should be kept simple and that the objective approach should remain: whether the stipulated sum is 'extravagant and unconscionable'.

- 19.15 *Single sum payable in a range of situations.* The claimant must take some care not to apply a single liquidated damages clause to deal with: (1) a contract containing a number of obligations which can be breached in a number of ways; or (2) a single obligation which might be breached in different ways and at different times so as to cause widely differing amounts of loss.⁴¹ However, these two sub-rules are presumptions, as *Dunlop Pneumatic Tyre Co. Ltd v. New Garage and Motor Co. Ltd* (1915) makes clear. They are not rigid rules. For example, in the *Dunlop* case, the relevant clause survived attack on this basis.⁴² But, in *Duffen v. FRA BO SpA* (1998), a clause was invalidated.⁴³

The clause in *Duffen v. FRA BO SpA* (1998) stipulated that, in the event of X being wrongly dismissed from his agency by Y, Y would pay X '£100,000 by way of liquidated damages which sum is agreed by the parties to be a reasonable pre-estimate of the loss and damage which the agent will suffer on termination of this agreement'. The Court of Appeal held that this was a penalty. It was not graduated to reflect the length of the unexpired term of the agency contract. The range of possible loss was £180,000 to £6,000 depending on the date of breach. Otton LJ described the stipulated sum as 'extravagant and unconscionable' and, on the facts, liable to confer a 'substantial windfall' upon X.

- 19.16 *Penalty in the context of money obligations.* A clause stipulating that non-payment of £x will require payment of £x and £y is a penalty (unless £y is a sum by way of interest set at a commercially acceptable level: see the *Jeancharm* case (2003) at 19.17). As Lord Dunedin said in the *Dunlop* case (1915):⁴⁴

It will be held to be a penalty if the breach consists only in not paying a sum of money, and the sum stipulated is a sum greater than the sum which ought to have been paid.

And, as Nicholls LJ explained in *Jobson v. Johnson* (1989):⁴⁵

Accordingly, once a court becomes aware that the amount claimed by the plaintiff is a penalty arising on default of payment of a specific sum of money the legal consequence which follows, as day follows night, is that the amount claimed will be scaled down by the court to a sum equal to the unpaid principal, with interest and costs.

41 *Dunlop Pneumatic Tyre Company v. New Garage* [1915] AC 79, 97–9, HL.

42 *Ibid.*, at 87.

43 *The Times*, 15 June 1998, CA.

44 *Dunlop* case, [1915] AC 70, 87, HL, *per* Lord Dunedin.

45 *Jobson v. Johnson* [1989] 1 WLR 1026, 1041, CA.

But, in the modern cases, some flexibility has been shown. Thus, Colman J in the *Lordsvale* case (1996) upheld a clause in a loan agreement which stipulated that the borrower's default in making repayments would trigger a *prospective* and 'modest' increase of one per cent in the level of interest.⁴⁶ Colman J admitted that this prospective increase was not a genuine pre-estimate of the loss. But he considered that the increase was justified and proportionate. This was because the borrower's default rendered that party a greater credit risk. It would have been different if the clause had provided that default would lead to a retrospective increase in the level of interest for the loan. In that situation, an increase in interest would apply to the whole period from the date of the loan. Such an increase would not be tailored to apply only from the date of default, which might occur at any stage in the currency of the loan.

- 19.17 The Court of Appeal in *Jeancharm Ltd v. Barnet Football Club Ltd* (2003) struck down as a penalty a clause stipulating that late payment of a commercial debt (the defendant club's liability for football shirts) would attract interest at the rate of 5 per cent per week.⁴⁷ This amounted to an annual rate of 260 per cent. This exorbitant rate of interest was intrinsically punitive. It could not be regarded as a genuine pre-estimate of loss (despite a desperate attempt by the payee's counsel to argue that the sum was intended to cover his client's 'administrative costs'). The court held that there was no need to show that the payee had oppressively exploited a commercially dominant position.
- 19.18 *Acceleration clauses.* An acceleration clause is not a penalty.⁴⁸ Such a clause works in this way. B's obligations consist of a series of payments by instalment. The clause states that, upon default, *all of these become payable in a lump sum*. And so B's overall liability is accelerated. In this situation, A is not regarded as having penalised B for breach. Instead, the courts take the view that the correct analysis is that B *can postpone performance of the lump sum obligation by making punctual instalment payments*. This approach to acceleration clauses can obviously produce hardship. However, as Woolf J observed in *Wadham Stringer Finance Ltd v. Meaney* (1981), Parliament has acknowledged the validity of acceleration clauses, referring to section 30(1) of the Hire-Purchase Act 1965.⁴⁹
- 19.19 *Consequence of finding a penalty.* A penalty clause is invalid beyond the amount of loss actually suffered. Thus, the party in breach is nevertheless liable to pay common law compensation if the innocent party can prove substantial loss. Furthermore, the penalty clause is not wholly void: instead, the clause cannot be enforced beyond the level

46 *Lordsvale Finance plc v. Bank of Zambia* [1996] QB 752, 763–7, Colman J (consistent with Canadian, Australian and New York banking law).

47 [2003] EWCA Civ 58; 92 Con LR 26.

48 *Wallingford v. Mutual Society* (1880) 5 App Cas 685, HL; *Protector Endowment Loan and Annuity Co. v. Grice* (1880) 5 QBD 121; *Wadham Stringer Finance Ltd v. Meaney* [1981] 1 WLR 39; *White and Carter (Councils) Ltd v. McGregor* [1962] AC 413, 426–7, HL.

49 [1981] 1 WLR 39, 48.

of true compensation. An action on a 'scaled down' penalty clause (its penal element having been excised) is technically a debt claim, rather than one for damages.⁵⁰ But, in practice, the penalty is regarded as a dead letter and the claim will instead be framed as one for common law damages based on general compensatory principles.⁵¹

- 19.20** *Valid liquidated damages clause acts as a cap.* If the amount payable under a valid liquidated damages clause turns out to be less than the loss suffered, the innocent party is bound by this figure. He cannot obtain greater compensation by suing for common law damages.

For example, in the *Cellulose Acetate Silk* case (1933),⁵² the contract concerned the construction of a factory. A clause stipulated that compensation for delay in completion would be at the rate of £20 per week. In fact, there was a thirty-weeks delay, and the actual loss suffered was £5,850, whereas the liquidated damages clause would yield only £600. The House of Lords held that the claimant was confined to £600, since the clause was not a penalty. Lord Atkin said that the parties had deliberately agreed to a clause which 'under-compensated' the innocent party. But it was not a pure limitation clause (that is, merely a financial cap on damages, but not imposing a minimum level of recovery: 15.01). Instead, the clause did impose a minimum level of recovery: and thus it was one which could have benefited the owners even if the loss suffered had been less than £20 per week.

As Burrows comments,⁵³ the courts should be slow to characterise an under-compensating clause as a liquidated damages clause which must be paid regardless of whether the payee will be favoured or disfavoured by the amount payable. His comment is sound because, in most situations, the more natural interpretation will be that the under-compensating clause was intended to provide for payment only if the payee suffered loss up to that amount. If it is characterised as a limitation clause, rather than as a 'two-way minimum and maximum payment clause', it might then be open to attack under the Unfair Contract Terms Act 1977 or the Unfair Terms in Consumer Contracts Regulations 1999 (on these statutory regimes, see 15.08 and 15.33).

- 19.21** *Invalid liquidated damages clause not a cap.* If the *under-compensating clause* (see preceding paragraph) is technically a *penalty* (for example, it fails to differentiate between different types of obligations which might be breached), the innocent party can sue at common law for damages to cover his greater loss. In this situation, the penalty provision has no effect,⁵⁴ even if the innocent party had inserted it into the contract.

50 *Jobson v. Johnson* [1989] 1 WLR 1026, 1039–41, CA, Nicholls LJ.

51 R. Halson, in M. Furmston (ed.), *The Law of Contract* (3rd edn, London, 2007), 8.125.

52 *Cellulose Acetate Silk Co. Ltd v. Widnes Foundry (1925) Ltd* [1933] AC 20, HL.

53 A. S. Burrows, *Remedies for Torts and Breach of Contract* (3rd edn, Oxford, 2004), 448–9.

54 *Jobson v. Johnson* [1989] 1 WLR 1026, 1039–41, CA, *per* Nicholls LJ.

In *Wall v. Rederiaktiebolaget Luggude* (1915),⁵⁵ Bailhache J invalidated a clause contained in a charterparty. The clause fixed the owner's liability under a charterparty to the amount of freight payable (on the facts, £1,125). In the event, the loss suffered by the charterer was £3,000. The judge held that the clause had not been intended to operate as a limitation clause. Instead, it was a penalty, both on its face and in substance (that is, a sum payable in the event of breach, without regard to the likely loss suffered; the amount was payable whether the loss turned out to be greater or less than the stipulated sum). And so, because the clause fell away as a penalty, the innocent party could ignore it and sue for his damages under common law principles.

This decision was approved by three members of the House of Lords in *Watts, Watts & Co. Ltd v. Mitsui & Co. Ltd* (1917)⁵⁶ (although this proposition's soundness was doubted by Lord Atkin in the *Cellulose* case (1933),⁵⁷ and by Diplock LJ in the *Robophone* case (1966)).⁵⁸ In view of this three-man support in the *Watts* case, it would be a bold thing for the English Court of Appeal to reverse this first instance decision. However, it must be admitted that it is odd that a party can invoke the penalty doctrine for the tactical purpose of escaping a *de facto* limitation of his liability even in the situation where he has freely agreed to that provision or perhaps even secured its inclusion. In the latter situation, the Supreme Court of Canada has held that the party stipulating for the penalty should not have the benefit of the limitation.⁵⁹ Burrows and Halson favour that approach.⁶⁰ But the counter-arguments are: (1) a clause is a penalty 'at birth' (the date of the contract's formation) irrespective of the amount of loss in fact suffered; and (2) the court should not be required to discover which party demanded that the clause be inserted.

- 19.22 Critique of the penalty doctrine (1).** Some commentators have criticised the penalty doctrine, suggesting that it is an unjustified fetter on the principle of freedom of contract (1.08).⁶¹ Admittedly, the law must protect *consumers* against liability to pay penalties.⁶² But here the Unfair Terms in Consumer Contracts Regulations 1999 (15.33) provide an adequate tool (the Regulations state that, if a term requires a consumer – confined to a 'natural person' – in breach of a contract to pay a 'disproportionately high sum in compensation' to a supplier of goods or services, this term will probably be regarded as unfair and so invalid).⁶³ 'Common law penalty critics' recognise the need for *statutory protection*

55 [1915] 3 KB 66, Bailhache J.

56 [1917] AC 227, 235, 245, 246, HL.

57 [1933] AC 20, 26, HL.

58 [1966] 1 WLR 1428, 1446, CA.

59 *Elsley v. JG Collins Insurance Agencies Ltd* (1978) 83 DLR (3d) 1, 14–15 (Supreme Court of Canada).

60 A. S. Burrows, *Remedies for Torts and Breach of Contract* (3rd edn, Oxford, 2004), 447–8; R. Halson, in M. Furmston (ed.), *The Law of Contract* (3rd edn, London, 2007), 8.126; A. H. Hudson, (1974) 90 LQR 31, (1975) 91 LQR 25, and (1985) 101 LQR 480; Gordon, (1974) 90 LQR 296; J. L. Barton, (1976) 92 LQR 20; W. F. Fritz, (1954) 33 *Texas Law Review* 196.

61 T. Downes, in P. B. H. Birks (ed.), *Wrongs and Remedies in the Twenty-First Century* (Oxford, 1996), 249, 265–6; M. Chen-Wishart, *ibid.*, at 279 ff; *Elsley v. JG Collins Insurance Agencies Ltd* (1978) 83 DLR 1, 15, Dickson J (Supreme Court of Canada).

62 T. Downes, in P. B. H. Birks (ed.), *Wrongs and Remedies in the Twenty-First Century* (Oxford, 1996), 249.

63 Schedule 2, paragraph 1(e) (an 'indicative' provision).

of consumers. But these critics would prefer that business parties should be free to fashion 'private sanctions'. If these critics were allowed to remould the law, therefore, the *judicial* penalty doctrine would be abolished. This would leave the 1999 Regulations as the only source of protection, and thus confined to contracts affecting consumers. Is this suggested remoulding of the law attractive?

19.23 *Rejoinder to the critics.* It is submitted that the common law penalty doctrine has a legitimate role. It should continue to apply both to consumer transactions and to *business-to-business transactions*. In general, monetary *punishment* is not an acceptable feature of contractual remedies. Such punishment will be appropriate only where the guilty party has seriously defied an injunction or order for specific performance, exposing himself to committal for contempt of court (18.13).

19.24 *Critique of the penalty doctrine (2): over-complicated rules.* The real criticism, it is submitted, is not that the judicial penalty doctrine survives, but that it has become so complex. In Victorian times, the rule could be stated relatively simply. But, nowadays, the case law has greatly complicated this doctrine. This can be contrasted with clear statements contained in foreign codes and 'soft law' transnational documents (although some English commercial lawyers might contend that these foreign statements are rather too brief). The *Principles of European Contract Law*, Article 9:509(2), states:

However, despite any agreement to the contrary the specified sum may be reduced to a reasonable amount where it is grossly excessive in relation to the loss resulting from the non-performance and the other circumstances.

UNIDROIT's *Principles of International Commercial Contracts* (2004), Article 7.4.13(2), provides:⁶⁴

However, notwithstanding any agreement to the contrary the specified sum may be reduced to a reasonable amount where it is grossly excessive in relation to the harm resulting from the non-performance and to the other circumstances.

The French *Code Civil*, Article 1152(2), provides:⁶⁵

The judge can, of his own motion or otherwise, diminish or increase the agreed penalty if it is manifestly excessive or derisory. Any provision in the contract to the contrary shall be deemed not to have been made.

⁶⁴ 2nd edn, Rome, 2004; see M. J. Bonell (ed.), *The UNIDROIT Principles in Practice: Case Law and Bibliography on the UNIDROIT Principles of International Commercial Contracts* (2nd edn, Ardsley, NY, 2006), 426 ff; S. Vogenauer and J. Kleinheisterkamp (eds.), *Commentary on the UNIDROIT Principles of International Commercial Contracts* (Oxford, 2009), 919 ff.

⁶⁵ B. Nicholas, *The French Law of Contract* (2nd edn, Oxford, 1992), 235–6; Scottish Law Commission, *Penalty Clauses* (Scottish Law Commission Report No. 171, Edinburgh, 1999) proposed a 'manifestly excessive' reformulation of the present doctrine.

3. RELIEF AGAINST FORFEITURE OF MONEY INSTALMENTS

- 19.25 Equity can relieve a party in breach against forfeiture of instalments already paid if the sum retained by the innocent party would be wholly disproportionate to the loss suffered by him as a result of the breach. The English authority supporting this is *Stockloser v. Johnson* (1954)⁶⁶ (see 19.26 for details), although the point was not directly decided in that case.
- 19.26 In the *Stockloser* case (1954), Denning and Somervell LJJs suggested that equity can relieve a party in breach against forfeiture of instalments already paid if the sum retained by the innocent party would be wholly disproportionate to the loss suffered by him as a result of the breach.⁶⁷ Denning LJ enunciated two criteria: the sum to be forfeited must be penal; and, secondly, its retention would be unconscionable.⁶⁸ These tests should be applied at the time of the claim, not at the earlier date of the transaction's formation.⁶⁹ It is submitted that Denning and Somervell LJJs's suggestion is attractive. The sums to be forfeited are not deposits in the strict sense (on deposits, see 19.27). The courts should be willing to discover whether the innocent party's retention of the sums would operate punitively and unfairly (on the analogy of the penalty jurisdiction, see 19.02).

4. DEPOSITS⁷⁰

- 19.27 A deposit is a valuable means of exerting pressure on the payor to comply with his contract. It is an 'earnest' payment. The penalty doctrine (19.02) does not apply to deposits, and so it makes no difference that a deposit is not a genuine pre-estimate of the vendor's likely loss.⁷¹ This means that the entire deposit can be validly forfeited even though that

66 [1954] 1 QB 476, CA; R. Goff and G. H. Jones, *The Law of Restitution* (7th edn, London, 2007), 20-041 ff, also noting, at 20-042, *Stern v. McArthur* (1988) 165 CLJ 489, High Court of Australia (on which see *Union Eagle Ltd v. Golden Achievement Ltd* [1997] AC 514, 522, PC: 17.40); L. Gullifer, in A. S. Burrows and E. Peel (eds.), *Commercial Remedies: Current Issues and Problems* (Oxford, 2003), 191, 205-12; and McGregor on Damages (18th edn, London, 2009), 13-098 ff; Meagher, Gummow and Lehane's *Equity: Doctrines and Remedies* (4th edn, Sydney, 2003), 18-130 ff.

67 [1954] 1 QB 476, 483-5, 490, CA.

68 *Ibid.*, at 490.

69 *Ibid.*, at 492.

70 R. Goff and G. H. Jones, *The Law of Restitution* (7th edn, London, 2007), 20-035 ff; K. Gray and S. F. Gray, *Elements of Land Law* (4th edn, Oxford, 2005), 12-46; L. Gullifer, in A. S. Burrows and E. Peel (eds.), *Commercial Remedies: Current Issues and Problems* (Oxford, 2003), 191, 205 ff; C. Harpum, [1984] CLJ 134-5, 163-6, 169-75; D. Harris, D. Campbell and R. Halson, *Remedies in Contract and Tort* (2nd edn, London, 2002), 58-61; 147-50; L. Ho, (2003) 119 LQR 34-9; McGregor on Damages (18th edn, London, 2009), 13-094 ff; A. J. Oakley, [1994] Conv 41; Law Commission, *Penalty Clauses and Forfeiture of Monies Paid* (Law Commission Consultation Paper No. 61, London, 1975); Meagher, Gummow and Lehane's *Equity: Doctrines and Remedies* (4th edn, Sydney, 2003), 18-080 to 18-125; G. H. Treitel, *Remedies for Breach of Contract: A Comparative Account* (Oxford, 1988), 234 ff.

71 *Workers Trust & Merchant Bank Ltd v. Dojap Investments Ltd* [1993] AC 573, 579, PC, per Lord Browne-Wilkinson; followed in *Polyset Ltd v. Panhandat Ltd* [2003] 3 HKLRD 319 (35 per cent deposit on commercial property held to be penal; compensation award substituted); L. Ho, (2003) 119 LQR 34.

innocent party's actual loss is less than the amount of the deposit (provided the deposit is not vulnerable to common law or statutory challenge: see 19.31 ff).⁷²

Forfeiture of a deposit given before the main agreement is reached, a 'pre-contract deposit', is subject to slightly different rules:⁷³ *prima facie*, the money can be reclaimed at any point from the payee or stakeholder;⁷⁴ but there can be an independent contract supported by consideration,⁷⁵ or perhaps even a non-contractual stipulation, rendering the pre-contract deposit irrecoverable if the payor does not enter the main contract, for reasons other than the payee's default.⁷⁶

- 19.28 Forfeiture of the deposit is justified if the payor fails without lawful excuse to fulfil the relevant transaction. The deposit will be lost when the purchaser manifestly abandons the contract, or clearly defaults, or if he delays in completing the sale to such a degree that the court can conclude that he has repudiated his contract.⁷⁷ Conversely, if the transaction goes smoothly, without the payor defaulting, the deposit will be put towards the purchase money. Of course, the payee must hand back the deposit if the contract came to an end as a result of his own default.⁷⁸ Finally, a prepayment cannot be forfeited if it was not paid as a deposit.

In *Mayson v. Clouet* (1924), the Privy Council held that forfeiture was restricted to a deposit of 10 per cent. The purchaser had made two further instalments, each of a further 10 per cent. He had then defaulted. The court held that only the first 10 per cent was a deposit, and that the further payments should be returned.⁷⁹

- 19.29 In principle, there should be no objection to the payee seeking compensation over and above⁸⁰ the amount of the deposit, unless the deposit is intended to place a cap on the payor's liability for breach. It is submitted that the normal construction should be that the deposit is an earnest payment and not a pre-estimate of the payor's total potential liability. It is also clear that, when calculating the amount of compensation for a breach, the fact that the innocent party has forfeited a deposit in relation to that breach must be taken into account when fixing the amount of compensation, otherwise the imposition of the deposit would be wholly penal and the award of

72 *Workers Trust & Merchant Bank Ltd v. Dojap Investments Ltd* [1993] AC 573, 578F, PC.

73 *Gribbon v. Lutton* [2001] EWCA Civ 1956; [2002] QB 902; considered in R. Goff and G. H. Jones, *The Law of Restitution* (7th edn, London, 2007), 20–36.

74 *Gribbon v. Lutton* [2001] EWCA Civ 1956; [2002] QB 902, at [14], approving Pennycuik V-C in *Potters v. Loppert* [1973] Ch 399, 405, 413.

75 *Gribbon v. Lutton* [2001] EWCA Civ 1956; [2002] QB 902, where all the judges accepted this possibility.

76 *Ibid.*, at [64], *per* Robert Walker LJ (attractive in principle, but not the basis of a clear and unanimous decision).

77 *Howe v. Smith* (1884) 27 Ch D 89, CA (delay justified forfeiture); cf the facts of *Cole v. Rose* [1978] 3 All ER 1121, 1129H.

78 *Cole v. Rose* [1978] 3 All ER 1121; C. Harpum, [1984] CLJ 134, 170.

79 [1924] AC 980, PC.

80 *Lock v. Bell* [1931] 1 Ch 35, Maugham J; *Shuttleworth v. Clews* [1910] 1 Ch 176.

compensation would be excessive because it would not accurately reflect the true extent of the loss.⁸¹

- 19.30 What if a deposit is owed (the duty to pay having ‘accrued’), but not paid? Can it be claimed by the party who (upon receipt) is entitled to ‘forfeit’ this sum? The answer is ‘yes, provided the contract has in fact ended through the payor’s default.’⁸² Furthermore, failure to pay a deposit can constitute a repudiatory breach of the contract, itself justifying termination of the contract,⁸³ at any rate if the vendor has re-notified the purchaser of the need to make this agreed payment.⁸⁴ Upon termination for breach in the situation just mentioned, the innocent party can obtain damages, and these can include the amount of the deposit.⁸⁵
- 19.31 *Sources of relief: introduction.* There are two possibilities for relief, although these will not necessarily apply to all contexts (for details of each, see the remainder of this chapter): (1) in contracts for the *sale or exchange of land* there is a *statutory* discretion to relieve against forfeiture of deposits;⁸⁶ and (2) there is a *common law* power to regulate excessive deposits; deposits of more than 10 per cent of the purchase price in contracts for the sale of land (or of a leasehold⁸⁷ interest) are normally⁸⁸ invalid (exceptionally, a larger deposit in a land transaction might be justified if there are ‘special circumstances’). If a deposit is excessive at common law, the deposit must be repaid, ‘less any damage actually proved to have been suffered as a result of non-completion’.⁸⁹
- 19.32 *Statutory relief to order repayment of deposits in the context of land transactions.* Section 49 of the Law of Property Act 1925 allows a court, ‘if it thinks fit’, to ‘order the repayment of any deposit’. But this provision applies only to contracts for the ‘sale or exchange of any interest of land’.⁹⁰
- 19.33 In the *Aribisala* case (2007),⁹¹ Alan Steinfield QC, sitting as a Deputy High Court Judge, held that this provision cannot be excluded by the parties’ agreement (for the sequel in

81 *Ng v. Ashley King (Developments) Ltd* [2010] EWHC 456 (Ch); [2010] 3 WLR 911, at [17] ff, especially at [51], *per* Lewison J.

82 *Damon Cia Naviera SA v. Hapag-Lloyd International SA* [1985] 1 WLR 435, 449G, 456F, CA; followed in *Ng v. Ashley King (Developments) Ltd* [2010] EWHC 456 (Ch); [2010] 3 WLR 911, at [36], [37], [51] and [52], *per* Lewison J.

83 *Ibid.*, at 446E, 456.

84 A. J. Oakley, [1994] Conv 41, 44, citing *Millichamp v. Jones* [1982] 1 WLR 1422, and *John Willmott Homes v. Read* [1985] 51 P & CR 90.

85 *Damon* case, [1985] 1 WLR 435, 449, 457, CA (Robert Goff LJ dissented).

86 Section 49(2) of the Law of Property Act 1925: see 19.32 ff.

87 E.g. *Maktoum v. South Lodge Flats Ltd*, *The Times*, 21 April 1980.

88 *Omar v. El-Wakil* [2001] EWCA Civ 1090; [2002] 2 P & CR 3 (at pp. 36 ff), CA (upholding a deposit of over 30 per cent in a conveyance of a business, both at common law and under section 49(2) of the 1925 Act; no citation of the *Workers Trust* case, see the next note).

89 *Workers Trust & Merchant Bank Ltd v. Dojap Investments Ltd* [1993] AC 573, 582, PC (citing *Commissioner of Public Works v. Hills* [1906] AC 368, PC).

90 Section 49(2)(3) of the 1925 Act.

91 *Aribisala v. St James Homes (Grosvenor Dock) Ltd (No. 1)* [2007] EWHC 1694 (Ch) (Alan Steinfield QC, sitting as a Deputy High Court Judge).

this litigation, see 19.34) because such an arrangement would be an attempt to oust the jurisdiction of the court and hence contrary to public policy (on this aspect of public policy, see 20.19).

19.34 The Court of Appeal in *Midill (97PL) Ltd v. Park Lane Estates Ltd and Gomba International* (2008) conducted a thorough review of the case law concerning section 49(2) of the 1925 Act. The following points emerge from Carnwath LJ's discussion.⁹²

A deposit is an earnest payment, and it follows that the court should be slow to offer relief to a defaulting party under this provision. Something exceptional is required. It will not be enough that the loss suffered by the vendor is less than the amount of the deposit. Nor, as on the facts of the *Midill* case, is it enough that the vendor has subsequently been successful in selling the property to a third party for a profit, because the market has risen during this time. However, the court acknowledged the soundness of Neuberger J's decision in the *Tennaro* case (2003)⁹³ to relieve the defaulting purchaser from forfeiture of his deposit on those facts (on this case, see below). Carnwath LJ in the *Midill* case summarised the decision in the *Tennaro* case as follows:⁹⁴

Three related contracts to grant long leases of three flats in the same block (Nos. 37, 32 and 31) were entered into between the vendor (Majorarch Ltd) and the purchaser (Tennaro Ltd). Deposits were paid in each case. The vendor served notices to complete in respect of the three contracts and, on the purchaser's failure to comply, purported to rescind each of the agreements and to forfeit the deposits.

Neuberger J rejected the [section 49(2)] claim for return of the deposit in respect of flat 37 (whose value had dropped by some £400,000), but allowed it for the other two flats. In respect of flat 32, the benefit of the agreement had been assigned to a third party, who had himself (at 'about the time that the contract with the buyer would have been completed') made an offer to purchase it for a price substantially higher than the contract price, which had been rejected by the vendor without explanation ...

In respect of flat 31, the buyer had been willing to purchase that flat alone at the purchase price, but the seller required it to be bought along with flat 37. Neuberger J concluded 'on balance' that in this case also the deposit should be repaid. He noted, in particular, that the seller had had the opportunity to complete at the contract price, and had not come forward with any explanation of this refusal; and ... that, on the basis of its then market value, the flat could have been resold at 15% above the contract price.

⁹² [2008] EWCA Civ 1227; [2009] 1 WLR 2460 (considering, especially, *Omar v. El-Wakil* [2001] EWCA Civ 1090; [2002] 2 P & CR 3 (at pp. 36 ff), CA; *Tennaro Ltd v. Majorarch* [2003] EWHC 2601; [2004] 1 P & CR 13, Neuberger J; and *Bidaisee v. Sampath* (1995) 46 WIR 461, PC, a case which had languished in obscurity).

⁹³ *Tennaro Ltd v. Majorarch* [2003] EWHC 2601; [2004] 1 P & CR 13, Neuberger J.

⁹⁴ [2008] EWCA Civ 1227; [2009] 1 WLR 2460, at [47] to [49].

Carnwath LJ then distinguished the present case as follows:⁹⁵

[The judge in the *Midill* case] was entitled to find that it was not enough that the vendor sold at a higher price some months after the date for completion. That delay distinguishes the case from the *Tennaro Ltd* case. There is nothing to suggest that the price rise [in the *Midill* case] was exceptional, in relation to movements in the market generally. There is no obvious reason why the purchaser should have the benefit of any such price rise. It was the vendor who had borne the risk and cost of holding the property during the intervening period. I also agree with the judge that to decide otherwise would add undesirable uncertainty to the well established contractual understanding.

- 19.35 *Common law jurisdiction to control excessive deposits.* In *Workers Trust & Merchant Bank Ltd v. Dojap Investments Ltd* (1993), the Privy Council affirmed that a deposit exceeding a 'reasonable' percentage is invalid at common law.⁹⁶

The case concerned a 25 per cent deposit relating to real property in Jamaica. Deposits between 15 per cent and 30 per cent were quite common in modern Jamaican land deals. Nevertheless, the Privy Council regarded these sums as unreasonably high. They were unacceptable deviations from the customary level of 10 per cent, which had long since been accepted within the UK and indeed in Jamaica.⁹⁷ *Prima facie*, the vendor should return the entire 25 per cent deposit. But the Privy Council held back a significant amount of the deposit as a 'fund' out of which any compensation due to the vendor should be paid.

- 19.36 The *Workers Trust* decision (1993) does not preclude a payee establishing 'special circumstances' justifying a deposit in excess of 10 per cent⁹⁸ if, say, the vendor might be exposed to high loss. But no such special case had been shown on the facts of that case.⁹⁹
- 19.37 Finally, the *Workers Trust* decision (1993) is easy to apply where a customary amount has emerged as the reasonable level (10 per cent in land transactions according to the Privy Council). But what if there is no such settled understanding, as in the case of deposits for the sale of chattels?¹⁰⁰ In *Vaswani v. Italian Motors* (1996), the Privy Council upheld a car seller's deposit of 25 per cent for a sports car to be built to the

⁹⁵ *Ibid.*, at [54].

⁹⁶ [1993] AC 573, PC (G. H. Jones and W. Goodhart, *Specific Performance* (2nd edn, London, 1996), 303–4; C. Harpum, [1993] CLJ 389; H. Beale, (1993) 109 LQR 524; M. Thompson, [1994] Conv 58).

⁹⁷ [1993] AC 573, 579, PC.

⁹⁸ *Ibid.*, at 580.

⁹⁹ *Ibid.*, at 581D–F.

¹⁰⁰ Beale, (1993) 109 LQR 524, 529.

purchaser's special order.¹⁰¹ The court did not suggest that the deposit might be attacked as unreasonable at common law. But, in a future case, it might be held that the common law jurisdiction to invalidate excessive deposits is applicable *even if* the transaction does not concern land. Where a transaction concerns a *consumer*, the Unfair Terms in Consumer Contracts Regulations 1999 will also apply (15.33).

¹⁰¹ [1996] 1 WLR 270, PC.

IX

Illegality and public policy

Chapter contents

1. Introduction *para. 20.01*
2. Agreements to commit a legal wrong *para. 20.06*
3. Agreements expressly or impliedly prohibited by statute *para. 20.07*
4. Gambling contracts no longer necessarily invalid *para. 20.10*
5. Public policy *para. 20.11*
6. Whether the claimant is sufficiently associated with the defendant's unlawful activity during performance *para. 20.22*
7. Consequences of illegality *para. 20.25*

20

The illegality doctrine

1. INTRODUCTION¹

20.01 Summary of main points

- (1) The long-standing illegality doctrine (the defence known as *ex turpi causa non oritur*: 20.03) has been applied to prevent a wrongdoer or wholly unmeritorious party from obtaining relief in the civil law. The courts (with the Law Commission's encouragement) have moved away from a mechanistic approach to this doctrine (for example, *Gray v. Thames Trains Ltd* (2009) and the *Stone & Rolls* case (2009)). They now consider whether denial of civil relief will be consistent with the policy underlying the relevant head of illegality or public policy (20.02 to 20.05).
- (2) Agreements are illegal, and hence unenforceable, if they involve an undertaking to commit a crime. An agreement is also illegal if the parties jointly and deliberately undertake to commit a legal wrong, such as a tort or breach of trust (20.06).
- (3) *Prima facie*, if statute (a) expressly or (b) by 'necessary implication' prohibits a transaction, neither party can enforce it, not even a party who is unaware of the relevant prohibition (*Re Mahmoud and Ispahani* (1921): 20.07). However, as for (a), a party intended to be protected by the statutory invalidity might be able to sue on the transaction (*Nash v. Halifax Building Society* (1979): 20.08); and, as for (b), in the absence of an express prohibition, the court will be reluctant to find an implied prohibition of a type of transaction if contractual invalidity within that context will operate harshly on a category of innocent parties (*Hughes v. Asset Managers plc* (1995): 20.08). Nor will the court find an implied prohibition of a type of transaction if

¹ *Chitty on Contracts* (30th edn, London, 2008), chapter 16; R. A. Buckley, *Illegality and Public Policy* (2nd edn, London, 2009); N. Enonchong, *Illegal Transactions* (London, 1998); for a wider perspective, see M. J. Trebilcock, *The Limits of Freedom of Contract* (Cambridge, MA, 1997).

the contract does not directly fall within the scope of the relevant statutory prohibition (*St John Shipping Corporation v. Joseph Rank Ltd* (1957): 20.09).

- (4) Following the Gambling Act 2005, gambling contracts are no longer illegal as such (although particular gambling offences can arise, and so affect gambling contracts, for example, where there is unlicensed commercial gambling or unlicensed use of premises for gambling purposes; and the Gambling Commission can declare particular bets to be void: 20.10).
- (5) In the absence of the invalidity summarised at (2) and (3) above, a contract can be invalidated because it is contrary to public policy. The effect is to deprive a party of the right to sue on the contract, and to entitle the other party to raise illegality as a defence to the contractual claim (20.11). The main heads of public policy are:
 - (a) contracts involving, or tending to promote, sexual immorality (*Pearce v. Brooks* (1866): 20.12);
 - (b) unacceptable agreements concerning matrimony (although this category of public policy is in a state of flux: 20.13);
 - (c) contracts involving physical or extreme economic servitude (20.14);
 - (d) contracts affecting public policy, notably transactions which involve trading with the enemy (20.15);
 - (e) contracts to deceive or cheat public authorities (20.16);
 - (f) contracts tending towards corruption in public office (20.17);
 - (g) contracts tending to pervert the course of justice (20.18);
 - (h) agreements to oust the court's jurisdiction (20.19); and
 - (i) agreements involving a restraint of trade (leading cases include: *Esso Petroleum Co. Ltd v. Harper's Garage (Stourport) Ltd* (1968) and *A Schroeder Music Publishing Co. Ltd v. Macaulay* (1974): 20.20 and 20.21).
- (6) If the contract is not expressly prohibited by statute, nor prohibited by necessary implication, and provided performance of the agreement will not necessarily entail illegality, a claimant is not disabled from suing on a contract if he has no knowledge of the defendant's illegal performance (*Archbalds (Freightage) Ltd v. S Spanglett Ltd* (1961): 20.22). Thus, the claimant is precluded from suing on the contract if he became aware that the contract will in fact be performed in an illegal fashion and he became implicated in that wrongdoing (*Ashmore, Benson, Pease & Co. Ltd v. AV Dawson Ltd* (1973): 20.23). What counts as 'implication', for this purpose, will depend on a range of factors (*Hall v. Woolston Hall Leisure* (2001) and *Anglo Petroleum Ltd v. TFB (Mortgages) Ltd* (2007): 20.24).
- (7) The consequences of illegality are summarised at 20.25 and 20.26. The main points are as follows:

- (a) Neither party can sue on a contract in situations of invalidity summarised at (2), (3) and (5) above.
- (b) But a claim upon a contract might not fail if the claimant was not aware of and implicated in the defendant's decision to perform it in an illegal fashion, as summarised at (6) above.
- (c) The claimant might have a separate action in tort for the defendant's deceit, or a valid claim for breach of a collateral contract.
- (d) The fact that possession in property has been acquired under an illegal contract does not preclude an action by the claimant owner to recover that property (or to obtain damages for conversion, in the case of chattels). Property can pass under an illegal contract by which title was intended to be transferred.
- (e) Sometimes, the court can sever an illegal portion of an overall transaction, and so give contractual effect to the lawful and uncontaminated part.
- (f) The court is entitled, indeed required, to refuse to give contractual effect to an illegal transaction even if its illegal nature only emerges incidentally during the conduct of the case.
- (g) Restitutionary consequences are summarised at 20.26.

Chitty on Contracts (30th edn, London, 2008), chapter 16

R. A. Buckley, *Illegality and Public Policy* (2nd edn, London, 2009)

N. Enonchong, *Illegal Transactions* (London, 1998)

Law Commission, *The Illegality Defence* (Law Commission Report No. 320, London, 2010), Part 3

Law Commission, *The Illegality Defence* (Law Commission Consultation Paper No. 189, London, 2009), Parts 3–5 (Part 3 contains a good overview of this topic, including reference to foreign legal systems and to the EU dimension)

Law Commission, *Illegal Transactions: The Effect of Illegality on Contracts and Trusts* (Law Commission Consultation Paper No. 154, London, 1999) (for an earlier discussion of the topic)

20.02 The Law Commission acknowledged (with understatement) that the law of illegality in contract law is 'an intricate web of tangled rules that are difficult to ascertain and distinguish'. As the Law Commission stated in its 1999 Consultation Paper,² legislation has not been recommended, other than in the context of illegality affecting proprietary interests under trusts law.³ Instead, in the field of contract law, the Law Commission,

² Law Commission, *The Illegality Defence* (Law Commission Consultation Paper No. 189, London, 2009), 1.14, 3.122.

³ On which see the recommendations in Law Commission, *The Illegality Defence* (Law Commission Report No. 320, London, 2010): this need for legislation is the 'fall-out' from the House of Lords' bare majority

in 2009, expressed the hope that the courts will develop a clearer statement of ‘the policies that underlie the illegality defence’ and allow that defence ‘to succeed only ... where it has some merit’.⁴ Recent case law in contract law (20.04, 20.05) and in tort (20.03) has followed the lead suggested by the Law Commission. Unless the relevant contract is expressly or by necessary implication invalidated by statute, the courts are prepared to make a sensitive inquiry whether underlying policy considerations justify barring a contractual claim. This is not a collapse of settled law into a loose discretion (as had been proposed in 1999),⁵ but rather elucidation of policies supporting the inherited body of law to ensure that those policies are properly applied, but not overplayed. What are those policies? The Law Commission’s 2009 Consultation Paper suggests this list:⁶

- (1) whether barring the claim will further the purpose underlying the offence or head of public policy;
- (2) whether allowing the claim will create unacceptable inconsistency between actionable civil rights and the relevant offence or head of public policy;
- (3) that the claimant should not be allowed to benefit, or perhaps make positive claims, in respect of his criminal or perhaps other serious wrongdoing;
- (4) whether the barring of the claim will send a salutary and appropriate deterrent message to others, similarly placed, that they should not commit the relevant offence or infringe the item of public policy;
- (5) whether barring the claim is appropriate or necessary in order to protect the civil process against abuse of its mechanisms;
- (6) possibly (this policy being the subject of intense dispute) whether the barring of the claim is appropriate in order to punish the claimant for his wrongdoing or moral turpitude.

Building on this list of policies, the Law Commission in 2009⁷ articulated various ‘factors’ that the court might consider when applying the existing law to particular contexts:

- (a) ‘whether the claim would undermine the purpose of the prohibiting rule’;
- (b) ‘the seriousness of the offence’;
- (c) ‘the causal connection between the claim and the illegal conduct’;

decision in *Tinsley v. Milligan* [1994] 1 AC 340, HL, to allow informal trusts to be validly asserted, notwithstanding the claimant’s illegality in conveying legal title to the transferee to make improper tax or social security arrangements, provided proof of the informal trust does not require the claimant to ‘rely’ on the forbidden or illegal transaction. In a work on contract law, it is permissible, and perhaps desirable, to end this note on trusts law quite abruptly.

4 Law Commission, *The Illegality Defence* (Law Commission Consultation Paper No. 189, London, 2009), 1.14.

5 ‘Illegal Transactions; the Effect of Illegality on Contracts and Trusts’ (L Com CP No. 154: 1999).

6 Law Commission, *The Illegality Defence* (Law Commission Consultation Paper No. 189, London, 2009), 2.5 to 2.29.

7 *Ibid.*, at 3.126 ff.

- (d) 'the comparative guilt of the parties'; and
- (e) 'the proportionality of denying the claim'.

The Law Commission concluded, first, that 'ultimately a balancing exercise is called for which weighs up the application of the various policies at stake'; and, secondly, the defence of illegality to a contractual claim should succeed 'only when depriving the claimant of his or her contractual rights is a proportionate response based on the relevant illegality policies'.⁸

20.03 As just noted, the Law Commission has usefully removed the lid from the illegality defence and encouraged the courts to identify the complex set of policies supporting that defence. The illegality defence has a long history (the so-called *ex turpi causa* maxim: see below). The defence is not confined to contract law.⁹ In the context of a tort action in the House of Lords in *Gray v. Thames Trains Ltd* (2009).¹⁰ Lord Hoffmann suggested that the *ex turpi causa* defence or principle cannot be reduced to a single criterion such as 'the claimant is precluded from success if he is obliged to rely on his own wrongdoing', and instead the doctrine operates in a more flexible fashion.¹¹

The maxim *ex turpi causa* expresses not so much a principle as a policy. Furthermore, that policy is not based upon a single justification but on a group of reasons, which vary in different situations.

The *Gray* case concerned a claim for lost earnings, and other damages, stemming from the claimant's imprisonment for homicide. He had killed a pedestrian, with whom he had had an argument, by running to a relative's nearby flat, grabbing a kitchen knife, chasing the pedestrian, and stabbing him. This willingness to kill in response to trivial provocation had been triggered by the trauma of a train crash, two years before (the Ladbroke Grove rail disaster), in which the claimant had been injured. That injury was the result of the defendant train company's negligence (Lord Hoffmann explained in detail the tragic chain of events).¹² The House of Lords unanimously held that the *ex turpi causa* principle precluded Gray's claim for damages. The claimant's act of criminal homicide was voluntary conduct for which he was responsible. The law could not offer compensation for the economic or other loss consequent upon the claimant's conviction and imprisonment for that criminal wrong.

⁸ *Ibid.*, at 3.142.

⁹ E.g. in *Safeway Stores v. Twigger* [2010] EWHC 11 (Comm); [2010] 3 All ER 577 the defence was considered in the context of claims pleaded as breach of contract, breach of fiduciary duty, and negligence (claim for compensation by company in respect of anti-competitive conduct committed by its employees; claimant incurring penalties under the Competition Act 1998; defence unlikely to succeed at trial, *per* Flaux J, because claimant was not personally responsible for employees' activity on these facts).

¹⁰ [2009] UKHL 33; [2009] 1 AC 1339 (noted by Paul S Davies (2009) 125 LQR 557).

¹¹ *Ibid.*, at [30].

¹² *Ibid.*, at [20] to [23].

20.04 In *Stone & Rolls Ltd v. Moore Stephens* (2009),¹³ a majority of the House of Lords (Lords Phillips, Brown and Walker) held that the *ex turpi causa* principle prevented the liquidator of a company from successfully suing, either in contract or in the tort of negligence, auditors who had negligently failed to identify the fact that the company was being run as a 'one man company' by a fraudster. The losses allegedly suffered by the company could not, therefore, be recovered as damages against the defendant auditor. Lord Phillips began by noting the general *ex turpi causa* principle:¹⁴

The policy underlying *ex turpi causa* was explained by Lord Mansfield CJ in 1775 in *Holman v. Johnson* (1775) 1 Cowp 341, 343:

'The objection, that a contract is immoral or illegal as between plaintiff and defendant, sounds at all times very ill in the mouth of the defendant. It is not for his sake, however, that the objection is ever allowed; but it is founded in general principles of policy, which the defendant has advantage of, contrary to the real justice, as between him and the plaintiff, by accident, if I may so say. The principle of public policy is this: *ex dolo malo non oritur actio*. No court will lend its aid to a man who founds his cause of action upon an immoral or an illegal act. If, from the plaintiff's own stating or otherwise, the cause of action appears to arise *ex turpi causa*, or the transgression of a positive law of this country, there the court says he has no right to be assisted. It is upon that ground the court goes; not for the sake of the defendant, but because they will not lend their aid to such a plaintiff. So if the plaintiff and defendant were to change sides, and the defendant was to bring his action against the plaintiff, the latter would then have the advantage of it; for where both are equally in fault, *potior est conditio defendentis*.'

The policy can be subdivided into two principles in relation to contractual obligations. (i) The court will not enforce a contract which is expressly or impliedly forbidden by statute or that is entered into with the intention of committing an illegal act. (ii) The court will not assist a claimant to recover a benefit from his own wrongdoing. This extends to claims for compensation or an indemnity in respect of the adverse consequences of the wrongdoing: see *Beresford v. Royal Insurance Co. Ltd* (1938).¹⁵

20.05 In its 2010 report, *The Illegality Defence*, the Law Commission suggested that the courts are now moving away from a 'mechanistic' application of the illegality bar.¹⁶ The Commission said that the House of Lords' *Gray* and *Stone & Rolls* cases (both 2009: see above), as well as subsequent High Court decisions,¹⁷ indicate that the courts are

13 [2009] UKHL 39; [2009] 1 AC 1391 (noted by P. Watts, (2010) 126 LQR 14–20; and D. Halpern, (2010) 73 MLR 487; considered in *Safeway Stores v. Twigger* [2010] EWHC 11 (Comm); [2010] 3 All ER 577 on the issue of corporate liability).

14 [2009] UKHL 39; [2009] 1 AC 1391, at [26].

15 [1938] AC 586, HL.

16 'The Illegality Defence' (Law Commission No. 320: 2010), 1.11 ff, especially 3.10 ff.

17 *Nayyar v. Denton, Wilde Sapte* [2009] EWHC 3218, Hamblen J, and *K/S Lincoln v. CB Richard Ellis Hotels Ltd* [2009] EWHC 2344.

adopting a more transparent style of reasoning to support their conclusion, referring to factors such as the need for deterrence and the triviality or otherwise of the wrong.

2. AGREEMENTS TO COMMIT A LEGAL WRONG

- 20.06 Agreements are illegal, and hence unenforceable, if they involve an undertaking to commit a crime (certainly if both are conspiring to commit a deliberate wrong,¹⁸ but perhaps also even if neither party is aware of the criminality,¹⁹ although this aspect of the law is not clear).²⁰ Indeed, an agreement to commit a crime is invalid, and the agreement itself constitutes the criminal wrong of conspiracy. If the parties had not at first committed themselves to an unlawful purpose, the courts will be prepared to examine whether there was a possibility of the contract being performed in a lawful fashion.²¹ An agreement is also illegal if the parties jointly and deliberately undertake to commit a legal wrong, such as a tort or breach of trust. But, if one party was unaware that contractual performance would involve a *civil wrong*, the better view is that he is entitled to recover the relevant fee, etc., for the whole of his performance, and not just for that part which was not unlawful. This is Treitel's²² attractive suggestion concerning a loose end within *Clay v. Yates* (1856),²³ where a publisher was entitled to payment for the work he had done before he realised that the remaining part of the job would involve a libel upon a third party. Furthermore, payment cannot be obtained if it was made conditional on performance of an unlawful act. At the time of *Beresford v. Royal Insurance Co. Ltd* (1938),²⁴ suicide was a crime. The life insurance policy in that case covered suicide. It was held that the successful suicide's estate could not claim insurance on this policy.²⁵

18 E.g. *Taylor v. Bhail* [1996] CLC 377, CA (headmaster of school and builder agreeing to inflate apparent price of repair work by £1,000; in return, builder awarded the job; builder's action for unpaid part of price failed both in contract law, because of illegal arrangement to defraud insurance company, and in restitution law, because he was party to the scam).

19 *JM Allan (Merchandising) v. Cloke* [1963] 2 QB 340, 348, CA, *per* Lord Denning MR (roulette wheel hired by defendant initially for an unlawful purpose, although neither party was aware of this; owner of wheel unable to claim for hire; wheel had been returned by defendant); noted by Law Commission, *Illegal Transactions: The Effect of Illegality on Contracts and Trusts* (Law Commission Consultation Paper No. 154, London, 1999), 2.20.

20 Law Commission, *Illegal Transactions: The Effect of Illegality on Contracts and Trusts* (Law Commission Consultation Paper No. 154, London, 1999), at 2.22. noting the contrary suggestion by Pearce LJ in *Archbolds (Freightage) Ltd v. S Spangle Ltd* [1961] 1 QB 374, 387, CA.

21 *Waugh v. Morris* (1873) LR 8 QB 202.

22 *Treitel* (12th edn, London, 2007), 11-017.

23 (1856) 1 H & N 73.

24 [1938] AC 586, HL.

25 Now the problem would not arise, because the Suicide Act 1961 decriminalised suicide; however, for the continuing problem concerning suicide pacts, and the crime of aiding and assisting suicide, see *Dunbar v. Plant* [1998] Ch 412, CA (limited scope for statutory relief against forfeiture of benefits obtained from the successful suicide's estate by the unsuccessful attempted suicide); applied in *Glover v. Staffordshire Police Authority* [2006] EWHC 2414 (Admin); [2007] ICR 661.

3. AGREEMENTS EXPRESSLY OR IMPLIEDLY PROHIBITED BY STATUTE

- 20.07 An agreement might sometimes be prohibited, whether expressly or by ‘necessary implication’,²⁶ by statute. If so, the result is that neither party can enforce it, not even a party who is unaware of the relevant prohibition (for possible escape from this, see 20.08). In *Re Mahmoud and Ispahani* (1921),²⁷ statute required licences for the sale and purchase of linseed oil. The defendant falsely told the plaintiff that he had a licence. In fact, only the plaintiff had a licence. When the defendant refused to accept delivery, the plaintiff sued for damages. The defendant successfully pleaded the defence of illegality. The Court of Appeal held that the defence, however unmeritorious on these facts (Bankes LJ described the defendant’s stance as ‘shabby’),²⁸ should prevail because the contract was expressly prohibited by the statute, unless both parties were licensed.
- 20.08 By contrast, Browne-Wilkinson J in *Nash v. Halifax Building Society* (1979)²⁹ held that a building society could recover money advanced under a contract of loan supported by a mortgage (the ‘second’ mortgage on the relevant property) even though statute³⁰ prohibited building societies from making loans on the security of property already subject to a mortgage or charge in favour of a third party. The judge said, with abundant common sense: ‘[T]he section is designed to protect the building society as a whole and, accordingly, although the transaction was illegal, the society is entitled to recover moneys advanced under such an advance and enforce the security given for its repayment.’ Similarly, the Court of Appeal in *Hughes v. Asset Managers plc* (1995) drew back from construing a statute, requiring investment contracts to be drawn up only by licensed investment agents, as an implied prohibition upon formation of the relevant contracts. Otherwise, as Saville LJ observed,³¹ the invalidity of all such contracts would have catastrophic consequences not only for investment companies (who might be expected in general to be capable of being diligent to avoid this hazard, and who are normally cash recipients) but, on the other side of this transaction, for investors, that is, institutions and ordinary members of the public. The same risk of total invalidity having an unmerited and harsh impact upon innocent non-professionals explains why the Financial Services and Markets Act 2000 enables insured persons (but not insurance companies) to sue on insurance contracts, where the relevant insurance business is transacted in breach of the regulatory system.³²

26 R. A. Buckley, ‘Implied Statutory Prohibition of Contracts’ (1975) 38 MLR 535.

27 [1921] 2 KB 716, CA (Atkin, Scrutton and Bankes LJ); similarly, the innocent claimant in *Chai Sau Yin v. Liew Kwee Sam* [1962] AC 304, PC, noted by Law Commission, *Illegal Transactions: The Effect of Illegality on Contracts and Trusts* (Law Commission Consultation Paper No. 154, London, 1999), 2.18.

28 [1921] 2 KB 716, 724, CA.

29 [1979] Ch 584, 591.

30 Section 32 of the Building Societies Act 1962.

31 [1995] 3 All ER 669, 674, CA.

32 Section 28 of the Financial Services and Markets Act 2000 (for the unfortunate case law background, notably, *Phoenix General Insurance Co. of Greece SA v. Halvanon* [1988] QB 216, 273, CA, which necessitated this change, see Law Commission, *The Illegality Defence* (Law Commission Consultation Paper No. 189, London, 2009), 3.101.

20.09 In other cases, the court has been asked to determine whether the relevant statutory offence impliedly prohibits a type of contract. In *St John Shipping Corporation v. Joseph Rank Ltd* (1957),³³ Devlin J held that a statutory offence did not entail implied prohibition of the relevant contract. Here, the plaintiff shipper had been fined by magistrates for the statutory offence of overloading a ship, but the fine had not kept up with inflation. The defendant charterer, ostensibly *pour encourager les autres*, withheld some of the freight payable under the contract of carriage, pleading as a defence that the plaintiff's performance of the contract had been illegal. Devlin J declined to find that the contract had been impliedly prohibited. He said:³⁴

A court should not hold that any contract or class of contracts is prohibited by statute unless there is a clear implication, or 'necessary inference', that the statute so intended. If a contract has as its whole object the doing of the very act which the statute prohibits, it can be argued that you can hardly make sense of a statute which forbids an act and yet permits to be made a contract to do it; that is a clear implication. But unless you get a clear implication of that sort, I think that a court ought to be very slow to hold that a statute intends to interfere with the rights and remedies given by the ordinary law of contract. Caution in this respect is, I think, especially necessary in these times when so much of commercial life is governed by regulations of one sort or another, which may easily be broken without wicked intent.

The preceding passage, therefore, concerned Devlin J's decision that the statute did not by necessary implication prohibit this type of contract. But he also held that there was no reason to invalidate the claim for freight merely because the plaintiff had knowingly performed the contract in an illegal fashion. He argued that it could not be shown that the defendant's cargo had itself directly led to the overloading.

4. GAMBLING CONTRACTS NO LONGER NECESSARILY INVALID³⁵

20.10 Part 17 ('Legality and Enforceability of Gambling Contracts') of the Gambling Act 2005 took effect on 1 September 2007. Section 335 of the Act, and associated provisions, repeal the numerous statutes which had invalidated such transactions. The new provision states:³⁶

(1) The fact that a contract relates to gambling shall not prevent its enforcement.

(2) Subsection (1) is without prejudice to any rule of law preventing the enforcement of a contract on the grounds of unlawfulness (other than a rule relating specifically to gambling).

³³ [1957] 1 QB 267.

³⁴ [1957] 1 QB 267, 289; for similar remarks on the proliferation of statutory offences of varying heinousness and technicality, see *Shaw v. Groom* [1970] 2 QB 504, 523, CA, *per* Sachs LJ.

³⁵ *Smith & Monkcom: The Law of Gambling* (3rd edn, Haywards Heath, 2009).

³⁶ Section 335 of the Gambling Act 2005.

'Gambling'³⁷ embraces 'gaming' (a 'game of chance for a prize'),³⁸ 'betting'³⁹ and participation in a 'lottery'.⁴⁰ The position can be summarised as follows. Gambling contracts are no longer illegal as such. But a gambling transaction might contain some other element which renders the transaction unlawful. That illegal element might arise (1) under the Gambling Act 2005 itself, which creates offences for unlicensed commercial gambling and unlicensed use of premises for gambling purposes;⁴¹ or (2) outside the statute, for example, where gambling is linked sufficiently with arrangements for the provision of prostitution (on that context, see 20.12). In addition, the 2005 Act empowers the Gambling Commission to declare particular bets to be void,⁴² in which case any stake or winnings can be recovered as a debt from the payee.⁴³

5. PUBLIC POLICY

- 20.11 Other contracts can be invalidated because the agreement is contrary to public policy (regarded by some as an 'unruly horse', but by others as a horse that can be mastered by a skilled rider). Lord Denning was not slow to proclaim his equestrian skills, for this purpose:⁴⁴

I know that over 300 years ago Hobart CJ said that 'Public policy is an unruly horse'. It has often been repeated since. So unruly is the horse, it is said [*per* Burrough J in *Richardson v. Mellish* (1824) 2 Bing 229, 252], that no judge should ever try to mount it lest it run away with him. I disagree. With a good man in the saddle, the unruly horse can be kept in control. It can jump over obstacles. It can leap the fences put up by fictions and come down on the side of justice.

Where public policy invalidates a transaction, the effect, once again, is to deprive a party of the right to sue on the contract, and to entitle the other to raise illegality as a defence to the contractual claim. The main heads of public policy are set out in 20.12 to 20.20.

- 20.12 *Contracting involving, or tending to promote, sexual immorality.* In *Pearce v. Brooks* (1866),⁴⁵ the plaintiff coachbuilders could not recover hire charges in respect of its horse-drawn carriage, nor claim compensation for damage caused to this carriage. It had been let in a state which was 'curiously constructed' to enable the defendant, a prostitute, to attract clients. It was enough that the plaintiff knew that the contract involved assistance in her 'immoral calling'. There was no need for the parties to have agreed that the hire would be paid directly from the prostitute's illicit earnings. Martin B explained:⁴⁶

³⁷ Section 3, *ibid.*

³⁸ Section 6, *ibid.*

³⁹ Section 9, *ibid.*

⁴⁰ Sections 14, 15, *ibid.*

⁴¹ Sections 33, 37, *ibid.*

⁴² Section 336(1), *ibid.*

⁴³ Section 336(2), *ibid.*

⁴⁴ *Enderby Town FC Ltd v. Football Association* [1971] Ch 591, 606–7, CA, *per* Lord Denning MR.

⁴⁵ (1866) LR 1 Exch 213, Court of Exchequer, Pollock CB, Martin, Pigott and Bramwell BB.

⁴⁶ *Ibid.*, at 219.

The [defence] states first the fact that the defendant was to the plaintiffs' knowledge a prostitute; second, that the brougham was furnished to enable her to exercise her immoral calling; third, that the plaintiffs expected to be paid out of the earnings of her prostitution. In my opinion the plea is good if the third averment be struck out; and if, therefore, there is evidence that the brougham was, to the knowledge of the plaintiffs, hired for the purpose of such display as would assist the defendant in her immoral occupation, the substance of the plea is proved, and the contract was illegal.

In *Coral Leisure Group Ltd v. Barnett* (1981),⁴⁷ Barnett brought a claim for unfair dismissal against a casino company. In his written claim, Barnett had alleged (*potentially* self-defeatingly, but see below) that part of his duties was to pay for prostitutes to be used by the casino's rich clientele. But the Employment Appeal Tribunal held that he had not thereby defeated his claim for unfair dismissal: the illegal element in the performance of this contract did not render the entire contract invalid for illegality. It would be different if: (1) the contract had been prohibited by statute, or (2) the parties to the contract had formed, from the beginning, the intention of pursuing this illegal purpose. In the absence of (1) or (2), Browne-Wilkinson J held that the contract could be asserted by the employee.

- 20.13 *Unacceptable agreements concerning matrimony.* There are two types of agreement concerning matrimony which historically have been unenforceable on the ground of public policy, namely, a marriage brokerage agreement, and an ante-nuptial agreement. The former remains unenforceable; the latter is no longer so.

Hermann v. Charlesworth (1905)⁴⁸ recognises that a marriage brokerage agreement (that is, an agreement to find a potential spouse for a fee) is contrary to public policy. This remains law, although it appears to be archaic. But mere 'dating agency' services are outside the scope of this rule and hence not unlawful.

Ante-nuptial and post-nuptial agreements concerning future property arrangements between spouses or prospective spouses, in the event of future separation, are no longer contrary to public policy. The Supreme Court in *Granatino v. Radmacher* (2010)⁴⁹ declared that such an agreement is no longer contrary to public policy. However, the most common context will concern the impact of such an agreement on the matrimonial jurisdiction to make property orders consequent on divorce. In that context, the agreement will inform exercise by the court of the discretion concerning property distribution, although the court will not be mechanically bound by the agreement when making this decision. This is so for three reasons.

47 [1981] ICR 503, 509, EAT, and later cases; on this troublesome line of cases, see Law Commission, *The Illegality Defence* (Law Commission Consultation Paper No. 189, London, 2009), 3.37 to 3.42, and S. Forshaw and M. Pigerstorfer, (2005) 34 ILJ 158.

48 [1905] 2 KB 123, CA.

49 [2010] UKSC 42; [2010] 3 WLR 1367.

First, the court has the ultimate statutory discretion as to how property should be distributed upon divorce, in accordance with sections 23–25 of the Matrimonial Causes Act 1973. The majority expressed this conclusion as follows:

If parties who have made such an agreement, whether ante-nuptial or post-nuptial, then decide to live apart, we can see no reason why they should not be entitled to enforce their agreement. This right will, however, prove nugatory if one or other objects to the terms of the agreement, for this is likely to result in the party who objects initiating proceedings for divorce or judicial separation and, arguing in ancillary relief proceedings [governed by the discretionary regime of sections 23–25 of the [Matrimonial Causes Act 1973] that he or she should not be held to the terms of the agreement ...

We do not consider it material in English ancillary relief proceedings whether the nuptial agreement under consideration is or is not a contract. The court can overrule the agreement of the parties, whether contractual or not, and applies the same criteria when considering whether to do so.⁵⁰

Secondly, the court might decide that an ante-nuptial (or indeed a post-nuptial) agreement was the product of improper influence (widely defined);⁵¹ or, thirdly, the court might decide that there has been a significant change of circumstances since the agreement was made.⁵² Finally, there is the overriding need to ensure that the agreement does not operate to the prejudice of children of the marriage.⁵³

Baroness Hale dissented in some respects (see below). But she also supplied the following (non-dissenting) exposition of the current law:⁵⁴

To sum up the position relating to agreements between husband and wife:

- (1) There is nothing to stop husbands and wives from making legally enforceable agreements about their property and finances which are to operate while they are living together, subject to the normal contractual requirements [on her comment concerning *Balfour v. Balfour* in this respect, see 6.09].
- (2) There is nothing to stop husbands and wives who are on the point of separating, or who are already separated, from making legally enforceable agreements about their financial rights and obligations while they are living apart.
- (3) ... [T]here is also nothing to stop husbands and wives who are not yet separated from making legally enforceable agreements about their financial rights and obligations while they are living apart.
- (4) However, the court has power to vary the financial arrangements for their separation, made in agreements between husbands and wives, under sections 35 and 36 of the [Matrimonial Causes Act 1973].

⁵⁰ *Ibid.*, at [52] and [74].

⁵¹ *Ibid.*, at [71] and [72].

⁵² *Ibid.*, at [81] and [82].

⁵³ *Ibid.*, at [77].

⁵⁴ *Ibid.*, at [154].

- (5) None of these agreements can oust the jurisdiction of the court to make financial orders should the parties separate or divorce.
- (6) Even if the parties have agreed what the court's order should be, the order derives its authority from the court and not from the parties' agreement.
- (7) The court therefore has its own independent duty to check the arrangements agreed between the parties and to evaluate them in the light of its statutory duties under section 25 of the [Matrimonial Causes Act 1973].

However, in the dissenting passages of her judgment, Baroness Hale suggested that the majority's judgment did not persuade her in these five respects:

- (1) In her view, there is no sound reason to treat ante-nuptial and post-nuptial agreements as equally deserving of legal validity. In her opinion, ante-nuptial agreements are especially likely to be the product of one-sided pressure and inequality.⁵⁵
- (2) She would have preferred this topic to be resolved not by judicial decision but by legislation, following careful review by the Law Commission.⁵⁶
- (3) In her opinion, the majority's decision in this case placed an 'impermissible gloss' upon the courts' statutory duties under the Matrimonial Causes Act 1973.⁵⁷
- (4) She disagreed with the majority's resolution of the present case on its facts.⁵⁸
- (5) She suggested (although this point is unlikely to prove correct) that ante-nuptial agreements have not ceased technically to be void at common law, and that the majority's suggestion that they are now legally valid was 'mercifully *obiter*',⁵⁹ whereas (contrary to Baroness Hale's suggestion) the majority's reasoning⁶⁰ clearly supports the independent legal validity of both ante-nuptial (a point decided in the *Granatino* case) and post-nuptial agreements (the latter agreements are no longer contrary to public policy, following the Privy Council's decision in the *MacLeod* case, 2008).⁶¹

See 6.09 on the presumption that there is no 'intent to create legal relations' if husband and wife make financial arrangements while the marriage is intact, and they have yet to separate (although a deed can be used to circumvent this difficulty, as the *MacLeod* case, above, itself illustrates).

20.14 *Servitude.* An agreement to enslave oneself will be contrary to public policy. In *Horwood v. Millar's Timber and Trading Co. Ltd* (1916),⁶² a borrower, Bunyan, agreed that, until the loan was repaid, he would pay *all* his earnings towards repayment, and furthermore

⁵⁵ *Ibid.*, at [162].

⁵⁶ *Ibid.*, at [133] to [135].

⁵⁷ *Ibid.*, at [166].

⁵⁸ *Ibid.*, at [193].

⁵⁹ *Ibid.*, at [138].

⁶⁰ *Ibid.*, at [52].

⁶¹ *MacLeod v. MacLeod* [2008] UKPC 64; [2010] 1 AC 298.

⁶² [1916] 2 KB 44, Divisional Court; P. Saprai, 'The Principle against Self-Enslavement in Contract Law' (2009) 25 *Journal of Contract Law* 26.

that he would not take another job, and finally that he would not move house without the lender's permission. One can see how, from the lender's perspective, these were attractive precautions. But Lush and Sankey JJ held that these severe restrictions offended the common law protection of the liberty to earn a living and the related freedom to move residence for that purpose. Therefore, the loan was illegal. At the time of the action, Bunyan had already enlisted for the Great War in 1914. The action was against his employer. It was for an account of all earnings and bonuses accruing in favour of the borrower, Bunyan, and payable by his employer (the loan agreement contained an assignment by Bunyan to the plaintiff lender of his earnings payable to him by the defendant). It would appear that the loan would also have been unenforceable against Bunyan (but, as mentioned, he was away at the front).

- 20.15 *Contracts affecting foreign policy.* Both at common law and by statute,⁶³ contracts involving trading with the enemy are contrary to public policy. The Trading with the Enemy Act 1939 (as amended) now defines 'enemy'.⁶⁴
- 20.16 *Agreements to deceive or cheat public authorities.*⁶⁵ In *Miller v. Karlinski* (1945),⁶⁶ the Court of Appeal held:

A contract of employment by which the employee is to be paid a specified weekly sum as salary and to recover from his employer the amount payable out of that sum in respect of income tax by including it in an account for travelling expenses is not severable, but the whole contract is illegal as being contrary to public policy and the courts will not entertain an action to enforce any of its terms. No action will therefore lie to recover arrears of salary alleged to be due.

In *Miller v. Karlinski* (1945), the plaintiff's claim for £71, which consisted of £50 for salary and the remainder for expenses, wholly failed. The plaintiff was not entitled to his salary because the illegal agreement as to sham travelling expenses was not a separate part of the contract.

The Court of Appeal in *Skilton v. Sullivan* (1994)⁶⁷ noted that an agreement is illegal if the parties have shared the purpose of avoiding or postponing VAT. However, no such shared purpose was present in that case, because the defendant was wholly innocent. Furthermore, the defendant could not satisfy the court that the claimant had formed the relevant wrongful intention (to postpone payment of VAT) at the time of the contract's formation. Although it was shown that the claimant had formed this illegal intention after the contract's formation, that did not preclude him from claiming the balance. And

⁶³ Trading with the Enemy Act 1939 (as amended).

⁶⁴ Section 2 of the Trading with the Enemy Act 1939 (as amended).

⁶⁵ See also the Bribery Act 2010.

⁶⁶ (1945) 62 TLR 85, CA; cf *Hall v. Woolston Hall Leisure* [2001] 1 WLR 225, CA (tax fraud; but employee aware but not a participant in the employer's fraudulent avoidance of tax and national insurance payments; employee not precluded from seeking compensation for sex discrimination); similarly, *Alexander v. Rayson* [1936] 1 KB 169, CA (fraud on rating authority).

⁶⁷ *The Times*, 25 March 1994.

so the court held that the claimant vendor was entitled to sue for the balance in respect of a supply of Koi carp.

- 20.17** *Contracts tending towards corruption in public office.*⁶⁸ In *Amalgamated Society of Railway Servants v. Osborne* (1910), the House of Lords held that an MP cannot contract with a third party that he will cast his vote in Parliament in a particular way.⁶⁹ In *Parkinson v. College of Ambulance Ltd* (1925),⁷⁰ an agreement foundered under this head because it involved payment for a knighthood. This type of sordid practice is now an offence.⁷¹ Similarly, an agreement to pay for improper influence in gaining a foreign government contract will offend English public policy. In an important discussion of this topic in *Lemenda Trading Co. Ltd v. African Middle East Petroleum Co. Ltd* (1988),⁷² Phillips J explained:⁷³

[I]t is possible to deduce the following principles underlying this head of public policy: (i) it is generally undesirable that a person in a position to use personal influence to obtain a benefit for another should make a financial charge for using such influence, particularly if his pecuniary interest will not be apparent. (ii) It is undesirable for intermediaries to charge for using influence to obtain contracts or other benefits from persons in a public position ...

It has certainly been a feature of the decided cases that the contract has involved influencing a decision to be taken by someone in a public position, though whether this feature is an essential element in the application of the doctrine has yet to be decided.

In some cases it will be difficult to decide whether this head of public policy applies so as to render a contract unenforceable. In certain circumstances the employment of intermediaries to lobby for contracts or other benefits is a recognised and respectable practice.

- 20.18** *Contracts tending to pervert the course of justice.* An agreement to procure false testimony⁷⁴ or to suppress evidence,⁷⁵ or to influence a juror or adjudicator will infringe this head of policy. Agreements to take a financial stake in the outcome of the proceedings or to share the fruits of a civil action (damages, etc.) remain contrary to common law (so-called ‘maintenance and champerty’).⁷⁶ However, the Courts and Legal Services Act

⁶⁸ See also the Bribery Act 2010.

⁶⁹ [1910] AC 87, HL.

⁷⁰ [1925] 2 KB 1, Lush J.

⁷¹ Honours (Prevention of Abuse) Act 1925.

⁷² [1988] QB 448.

⁷³ [1988] QB 448, 458.

⁷⁴ *R v. Andrews* [1973] QB 422, CA, *per* Lord Widgery CJ.

⁷⁵ *R v. Ali* [1993] Crim LR 396, CA (offence extends to agreement that potential witness should not give evidence); *R v. Panayiotou* [1973] 3 All ER 112, CA (attempt to procure dropping of charge).

⁷⁶ J. Sorabji and R. Musgrove, ‘Litigation, Costs, Funding, and the Future’, in D. Dwyer (ed.), *The Civil Procedure Rules Ten Years On* (Oxford, 2009), 229, at 235, examining the liberal tendency in the modern cases (e.g. *Arkin v. Borchard Lines Ltd* [2005] EWCA Civ 655; [2005] 1 WLR 3055, at [40]: a non-party ‘commercial funder’ of litigation brought by A was found liable to pay the victorious party B’s costs to the extent that the non-party provided finance in that litigation; funding agreement was not champertous).

1990 allows lawyers to agree to conduct a case on a no-win-no-fee basis. This has been the foundation for the growth of conditional fee agreements (a large topic, which the author has examined elsewhere).⁷⁷ The upshot is that a contract for legal services concerning civil litigation or arbitration can now validly render the lawyer's right to obtain a fee, or an increased fee, dependent on his client's success in obtaining a favourable judgment or settlement. In essence, a 'conditional fee agreement' permits a solicitor or barrister in England and Wales to undertake to perform litigation services on the understanding that his normal legal fee will not be payable if the client is unsuccessful in the relevant proceedings; but, if he achieves success for his client, the lawyer will receive an enhanced fee, consisting of his ordinary fee (normally, in the case of solicitors, this will be based on hourly charges) and a percentage of that fee (the percentage 'uplift' cannot exceed 100 per cent). In practice, the victorious lawyer's fee will be paid by the losing party (in accordance with the 'loser must pay' costs rule in English civil proceedings). However, such an agreement remains invalid, under the common law public policy prohibition if the relevant statutory formalities have not been satisfied.⁷⁸ This topic is in a state of flux following the recommendations in late 2009 of Lord Justice Jackson's *Review of Civil Litigation Costs: Final Report*.⁷⁹ His recommendation⁸⁰ is that US-style 'contingency fee agreements' (not the same as conditional fee agreements)⁸¹ should be valid, provided the client receives independent advice before agreeing to this fee arrangement.

- 20.19 *Agreements to oust the court's jurisdiction.* Such a contract is illegal (for an example, see the discussion at 19.33). But, in the case of arbitration agreements, the Arbitration Act 1996 upholds a written arbitration agreement⁸² and allows a party to seek a stay of English legal proceedings brought 'in respect of a matter which under the [arbitration] agreement is to be referred to arbitration'.⁸³ The court will grant a stay unless the arbitration agreement is 'null and void, inoperative, or incapable of being performed'.⁸⁴ As for points of English law determined by the arbitrator, the parties can agree that the arbitrator, in making his award, can 'dispense with reasons'. And so the parties can exclude the court's power to hear an appeal.⁸⁵ Subject to that, an appeal on a point of English law can be referred to the High Court, but only if the parties agree or if the court itself grants 'leave to appeal'. For this purpose, the High Court applies a restrictive set of 'filtering'

77 N. Andrews, *The Modern Civil Process* (Tübingen, 2008), 9.19 ff.

78 *Awwad v. Geraghty* [2001] QB 570, 596, CA, noted by N. Andrews, [2000] CLJ 265–7, and A. Walters, (2000) 116 LQR 371–7 (and not following *Thai Trading Co. v. Taylor* [1998] QB 781, CA, noted by N. Andrews [1998] CLJ 469).

79 December 2009: published 2010.

80 *Ibid.*, at 64.

81 US contingency fees give an American attorney an agreed percentage of the successful plaintiff's damages or settlement: N. Andrews, *The Modern Civil Process* (Tübingen, 2008), 9.27 ff.

82 Section 5 of the Arbitration Act 1996.

83 Section 9(1), *ibid.*

84 Section 9(5), *ibid.*

85 Section 69(1), *ibid.*

criteria.⁸⁶ The Act's definition of matters of 'law' is confined to English law. This places findings of foreign law beyond the scope of High Court appeal.⁸⁷

20.20 *Agreements involving a restraint of trade.*⁸⁸ The courts eschew any general power to invalidate terms or contracts on the ground of reasonableness. But, where an arrangement unreasonably stultifies a person's legitimate interest in pursuing a trade or profession, or otherwise engaging in useful economic activity, the doctrine of 'restraint of trade' can invalidate the offending provision (which might be an entire agreement, a free-standing clause, or at least part of a clause which can be excised using the process of 'severance',⁸⁹ leaving the remaining portion of the clause operative). The law on this topic is highly detailed, and only a sketch can be provided here. Employment contracts (the doctrine can extend to other forms of association) might provide that upon ceasing to be an employee the former employee will not exploit his ex-employer's trade secrets, or confidential information, or solicit custom from the contacts acquired by the employee during his employment with the covenantor (the employee is only released from such a restrictive covenant if he is wrongly dismissed by the employer).⁹⁰ Another well-established form of restraint of trade arises when the seller of a business, transferred along with its goodwill (the benefit of its established client base), agrees with the purchaser not to carry on a business which will compete with the buyer's newly acquired business. Thirdly, in various other commercial contexts, an agreement might unacceptably preclude a party from exercising a freedom that he might otherwise have. For example, in *Esso Petroleum Co. Ltd v. Harper's Garage (Stourport) Ltd* (1968),⁹¹ the House of Lords struck down a twenty-one-year solus agreement which required the petrol retailer, the owner of the site, not to buy fuel from anyone other than Esso. In return, the retailer received a reduction in the wholesale price. But, in the same litigation, it was held that a four-year solus agreement was acceptable: the petrol company was justified, for that period, in protecting its interest by securing a reasonable degree of continuity in its supply to retailers. The reader is referred to a long passage in Lord Reid's speech where these matters are explained.⁹²

In *A Schroeder Music Publishing Co. Ltd v. Macaulay* (1974),⁹³ the House of Lords invalidated a music agency agreement under which a 21-year-old songwriter agreed to assign copyright in all his songs composed during the next five years. The agreement could be extended to ten years if his royalties exceeded £5,000 in the first period. The publisher was not obliged to publish his works. Although the songwriter was committed to the contract for five, or even ten years, the publisher could terminate the contract on

86 Section 69(3), *ibid.*

87 Section 82(1), *ibid.*

88 J. D. Heydon, *The Restraint of Trade Doctrine* (3rd edn, Chatswood, 2009); M. J. Trebilcock, *The Common Law of Restraint of Trade – A Legal and Economic Analysis* (Toronto, 1986); S. Smith, 'Reconstructing Restraint of Trade' (1995) 15 OJLS 565.

89 *Treitel* (12th edn, London, 2007), 11–151 ff.

90 *General Billposting Co. Ltd v. Atkinson* [1909] AC 118, HL (on which 17.48).

91 [1968] AC 269, HL.

92 *Ibid.*, at 301–3.

93 [1974] 1 WLR 1308, HL.

one month's notice. The songwriter, Macaulay, proved to be a success. He then obtained a declaration that the contract was void as contrary to public policy, because it was an unreasonable restraint of trade (no relief beyond this bare declaration is mentioned in the law report). The publisher failed to show that this restraint of trade could be justified as reasonable. Lord Reid explained:⁹⁴

In the present case the respondent assigned to the appellants 'the full copyright for the whole world' in every musical composition 'composed created or conceived' by him alone or in collaboration with any other person during a period of five or it might be ten years. He received no payment (apart from an initial £50) unless his work was published and the appellants need not publish unless they chose to do so. And if they did not publish he had no right to terminate the agreement or to have copyrights re-assigned to him. I need not consider whether in any circumstances it would be possible to justify such a one-sided agreement. It is sufficient to say that such evidence as there is falls far short of justification. It must therefore follow that the agreement so far as unperformed is unenforceable.

- 20.21 All covenants in restraint of trade must be justified as reasonable having regard to both (a) the interests of the contracting party and (b) the interests of the public. The covenant must be aimed at protecting the legitimate interests of the covenantee. In the case of the sale of a business, the buyer has a legitimate interest in protecting the integrity of the established client base – which it has bought – from being undermined by rival competition by the seller. But an employer has no legitimate interest in stopping its former employee from setting up a rival business. Instead, its protection is confined to its interests in protecting its trade secrets, or other confidential information, and in preventing the employee from filching his custom by taking advantage of customer details and contacts acquired during the period of employment. The employee's covenant cannot catch types of business different from the covenantee's. Nor must the covenant contain a restriction which is excessive in geographical scope. In *Mason v. Provident Clothing & Supply Co.* (1913), the restriction concerned work as a commercial canvasser within twenty-five miles of London (an area over 1,000 times larger than the employee's usual field of work), and this was held to be too broad.⁹⁵ Nor should the restriction endure too long.⁹⁶ Similarly, in cases concerning the sale of a business with goodwill, the length of the period of restraint and its area of operation must be reasonable. However, in one famous case, *Nordenfelt v. Maxim Nordenfelt Guns and Ammunition Co. Ltd* (1894), the sale of an armaments business contained a restrictive covenant preventing the vendor from engaging in rival trade for twenty-five years anywhere else in the world. The House of Lords held that this was not excessive, because the vendor, a Swedish millionaire arms manufacturer, had already achieved a worldwide sales base.⁹⁷

⁹⁴ *Ibid.*, at 1313–15, HL.

⁹⁵ [1913] AC 724, HL.

⁹⁶ A five-year period was held to be unreasonable in *M & S Drapers v. Reynolds* [1957] 1 WLR 9, CA.

⁹⁷ [1894] AC 535, HL.

6. WHETHER THE CLAIMANT IS SUFFICIENTLY ASSOCIATED WITH THE DEFENDANT'S UNLAWFUL ACTIVITY DURING PERFORMANCE

20.22 *Innocent party can sue if contract is not prohibited by statute and its performance does not necessarily involve unlawful conduct.* If the contract is not expressly prohibited by statute, nor by necessary implication, and provided performance of the agreement will not necessarily entail illegality, a claimant is not disabled from suing on a contract if he has no knowledge of the defendant's illegal performance. In *Archbolds (Freightage) Ltd v. S Spanglett Ltd* (1961),⁹⁸ the plaintiff had contracted for the defendant to transport goods by van, not knowing that the defendant's particular van was unlicensed for this purpose and that its use in this way would involve an offence. The plaintiff's goods were lost in transit (they were stolen as a result of the defendant's negligence), and the plaintiff sued for loss on the basis of contractual breach. The Court of Appeal rejected the defence based on illegality: this was not a case of a contract expressly or implied prohibited; nor had the parties jointly agreed to commit an offence or infringe public policy; nor, finally, had the plaintiff been aware that use of this particular van in this transaction would involve a criminal wrong. Pearce LJ explained:⁹⁹

[N]o case has been cited to us establishing the proposition that where a contract is on the face of it legal and is not forbidden by statute, but must in fact produce illegality by reason of a circumstance known to one party only, it should be held illegal so as to debar the innocent party from relief ... The plaintiffs were never *in delicto* [implicated in conscious wrongdoing] since they did not know the vital fact that would make the performance of the contract illegal.

20.23 *Inability to sue if claimant participates in unlawful performance.*¹⁰⁰ Although the contract is not prohibited by statute, nor does its performance necessarily involve unlawful conduct, the claimant will be unable to sue on it if he became aware that the contract will in fact be performed in an illegal fashion and he becomes implicated in that wrongdoing. He is then precluded by the defence of illegality from being able to enforce the contract. This was decided by the Court of Appeal in *Ashmore, Benson, Pease & Co. Ltd v. AV Dawson Ltd* (1973).¹⁰¹ In that case, the defendant agreed to transport the plaintiff's goods, but the defendant overloaded its lorry, contrary to statute. The defendant knew this was an offence. The plaintiff's goods were damaged when the lorry toppled over. The plaintiff's contractual claim for this loss failed. The plaintiff's manager had been implicated in the defendant's illegal performance: he knew that the loading involved breach of the relevant statute; indeed this had happened before; and, furthermore, the plaintiff company's

⁹⁸ [1961] 1 QB 374, CA.

⁹⁹ [1961] 1 QB 374, 387–8.

¹⁰⁰ An article antedating some of the case law examined in this paragraph is R. A. Buckley, 'Participation and Performance in Illegal Contracts' (1974) 25 *Northern Ireland Legal Quarterly* 421.

¹⁰¹ [1973] 1 WLR 828, CA.

connivance in this criminal activity enabled it to make a saving in its transport costs. As Lord Denning MR explained:¹⁰²

Mr Bulmer [the plaintiff's manager] must have known that these articulated lorries of Dawsons were only permitted to carry 20 tons. Nevertheless, realising that 25 tons was too heavy – much too heavy – for them, he was content to let them carry the loads because it had happened before without trouble. He was getting the transport done cheaper too by £30 saved on each trip by each load. Not only did Mr Bulmer know of the illegality. He participated in it by sanctioning the loading of the vehicle with a load in excess of the regulations. That participation in the illegal performance of the contract debars Ashmores from suing Dawsons on it or suing Dawsons for negligence.

20.24 In *Hall v. Woolston Hall Leisure* (2001),¹⁰³ Mance LJ suggested that the *ratio* of the *Ashmore* case involved not merely the claimant's knowledge of the criminal activity but participation in that wrongdoing, in the sense that the claimant was not merely turning a blind eye to the wrong, but collusively making a gain from this acquiescence. Similarly, in *Anglo Petroleum Ltd v. TFB (Mortgages) Ltd* (2007),¹⁰⁴ Mummery LJ noted that participation does not arise solely from knowledge of the other's criminal or unlawful use of the relevant object or service. If that were so, no one could sue on a contract to supply basic living items (food and ordinary clothing) to a prostitute. It appears, therefore, that the courts will have regard to the special nature of the goods or services supplied (the 'ornamental carriage' in *Pearce v. Brooks*: 20.12), whether the supplier is directly profiting from the defendant's illegal activity (as in the *Ashmore* case: 20.23), the heinousness of both the claimant's activity (repeated dealings, as in the *Ashmore* case) and that of the defendant's wrongdoing (for example, the liquidator of a former quarrying business sells detonators to suspicious laymen, and it turns out that they are terrorists).

7. CONSEQUENCES OF ILLEGALITY

20.25 There are nine main propositions.

- (1) Where the contract is expressly or by necessary implication prohibited by contract, neither party can sue on it (20.07 to 20.09).
- (2) The same applies where the contract is invalid because the common purpose of the transaction was to commit a crime or other (serious) legal wrong (20.06).
- (3) We have seen that the claim upon a contract might not fail if the claimant was not aware of and implicated in the defendant's decision to perform it in an illegal fashion (20.22; and compare a claimant's participation in an unlawful performance, 20.23).

¹⁰² [1973] 1 WLR 828, 833, CA.

¹⁰³ [2001] 1 WLR 225, at [80].

¹⁰⁴ *Anglo Petroleum Ltd v. TFB (Mortgages) Ltd* [2007] EWCA Civ 456; [2007] BCC 407 (acknowledging, however, that the law remains malleable: *ibid.*, at [73] to [82]).

- (4) Sometimes, the courts have found that, despite the invalidity of the principal contract, the claimant has a separate action for the tort of deceit¹⁰⁵ committed by the defendant, or that there is a valid claim for breach of a collateral contract.¹⁰⁶
- (5) The claimant might be entitled to a claim for recovery of money paid or for a *quantum meruit* in respect of services or a *quantum valebat* for goods delivered. The Law Commission has recently provided a detailed study of opportunities for restitution to avoid the defendant's unjust enrichment,¹⁰⁷ and a summary is provided in the next paragraph at 20.26.
- (6) The fact that possession in property has been acquired under an illegal contract does not preclude an action by the claimant owner to recover that property (or to obtain damages for conversion, in the case of chattels).¹⁰⁸
- (7) Property can pass under an illegal contract by which title was intended to be transferred.¹⁰⁹ The Law Commission has examined these last two topics.¹¹⁰
- (8) In some situations, the court can sever an illegal portion of a transaction, and thus give effect to the lawful and uncontaminated part of the transaction:¹¹¹
 - (a) The court will not sever parts of an undertaking if it perceives that they are in substance inextricably linked, and that severance would emit the 'wrong message' to the commercial community, by condoning an unacceptable practice. Thus, the Court of Appeal (having received supplementary argument from an intervenor, an *amicus curiae* appointed by the Treasury Solicitor) loudly censured the parties to a fraudulent building contract in *Taylor v. Bhail* (1996).¹¹² A defendant headmaster (of a private school) agreed with the claimant builder to inflate the invoice by £1,000 for repairs to the school buildings, provided the defendant could keep the extra £1,000. The effect was to raise the cost of the work from £12,000, the true cost, to £13,000. The building work would be financed by the defendant's insurer, which would be tricked into believing that the real cost of these works was £13,000. The Court of Appeal held that this was a conspiracy to defraud the third party insurer. Although the initiative for this

105 *Shelley v. Paddock* [1980] QB 384, 357, CA (defendant swindled the claimant into paying for property not in fact owned by defendant; but claimant had breached exchange-control rules; action based on defendant's fraudulent misrepresentation that he was owner permitted); for an argument that sometimes the defendant might be held to have assumed a tortious duty to save the claimant from the trap (known to, or reasonably ascertainable by, a more knowledgeable defendant), see N. Enonchong, [2000] *Restitution Law Review* 241, 250 ff.

106 *Strongman (1945) Ltd v. Sincok* [1955] 2 QB 525, CA (defendant refusing to pay for claimant's building work because licence not obtained for such work; defendant, an architect, had undertaken to obtain such a licence; main building contract invalid because unlicensed work; but defendant's collateral assurance, that licence would be obtained, enforceable and claimant able to recover payment for his work as damages for breach of that collateral warranty).

107 Law Commission, *The Illegality Defence* (Law Commission Consultation Paper No. 189, London, 2009), Part 4, at 65–85.

108 *Bowmakers Ltd v. Barnet Instruments Ltd* [1945] KB 65, CA.

109 *Singh v. Ali* [1960] AC 167, 176, PC; *Belvoir Finance Co. v. Stapleton* [1971] 1 QB 210, CA.

110 Law Commission, *The Illegality Defence* (Law Commission Consultation Paper No. 189, London, 2009), Part 5, at 86–93.

111 R. A. Buckley, *Illegality and Public Policy* (2nd edn, London, 2009), chapter 19.

112 [1996] CLC 377.

fraud had come from the defendant, the claimant had acquiesced and participated in it; otherwise, the defendant had made clear that the claimant would not have got the job. The court regarded this as the plainest example of an illegal element tainting the whole transaction; and it would be unacceptable to allow the builder to sue for the unpaid balance up to the level of £12,000.

Sir Stephen Brown P said:¹¹³

[T]he contract was, in substance, an agreement between the appellant and the respondent to defraud a third party, the insurance company. This ... is not capable of severance ... I believe this to be a very clear case, and the message should be sent out loud and clear that if parties conspire to defraud an insurance company, as in this case, they cannot expect the courts to assist them in implementing their agreement.

Russell LJ said:¹¹⁴

[T]he question, then arises whether the court will sever that part of the agreement dealing with the £1,000 from that part; namely the building work, which was lawful. In my view the two parts of the one agreement are inextricably intertwined; so there is no room for severance. The whole contract is therefore tainted by fraud, not a severable part of it.

Millet LJ said:¹¹⁵

This was a conspiracy to defraud. It is quite unrealistic to regard it as a building contract for £12,000 with a separate and independent agreement to defraud the defendant's insurers superimposed upon it.

- (b) As for textual severance of an illegal part of a written contract which is otherwise lawful, Treitel notes:¹¹⁶ (i) it is unclear whether this type of severance is possible outside the contexts of contracts in restraint of trade or agreements to exclude the court's jurisdiction; (ii) severance requires the possibility of clean¹¹⁷ textual excision; that is, the offending part can be removed allowing the lawful remainder to stand intact; textual rearrangement is not possible; (iii) severance must not alter the whole nature of the contract;¹¹⁸ furthermore (iv) '[i]t can hardly be imagined that a Court would enforce a promise, however inherently valid and however severable, if contained in a contract one of the terms of which

113 *Ibid.*, at 381.

114 *Ibid.*

115 *Ibid.*, at 382.

116 Treitel (12th edn, London, 2007), 11-158 to 11-163.

117 Illustrated by *Goldsoll v. Goldman* [1915] 1 Ch 292, CA (deleting geographical references without distorting overall grammatical sense of relevant sentence); for a slightly more flexible approach, see *T Lucas & Co. v. Mitchell* [1874] Ch 129, CA.

118 E.g. *Attwood v. Lamont* [1920] 3 KB 571, 577-8, CA, where Lord Sterndale MR made clear that this test arises in addition to the court's capacity to effect a 'blue-pencil' excision of an offending part of the text.

provided for assassination'.¹¹⁹ And it follows that the proposed severance must be assessed by considering the heinousness of the relevant transaction.

- (9) The court is entitled, indeed required, to refuse to give contractual effect to an illegal transaction even if its illegal nature only emerges incidentally during the conduct of the case. The Court of Appeal in *Birkett v. Acorn Business Machines Ltd* (1999) explained the matter as follows:¹²⁰

If a transaction is on its face, that is to say merely by looking at its terms and without additional evidence, manifestly illegal, the Court will refuse to enforce it, whether or not either party alleges illegality. If a transaction is not on its face manifestly illegal but there is before the Court persuasive and comprehensive evidence of illegality, the court may refuse to enforce it even if illegality has not been pleaded or alleged. The principle behind the court's intervention of its own motion in such a case is to ensure that its process is not being abused by inviting it to enforce *sub silentio* a contract whose enforcement is contrary to public policy. Thus, in *Re Mahmoud and Ispahani*, Scrutton LJ observed:¹²¹

'In my view the court is bound, once it knows that the contract is illegal, to take the objection and to refuse to enforce the contract, whether its knowledge comes from the statement of the party who was guilty of the illegality, or whether its knowledge comes from outside sources. The court does not sit to enforce illegal contracts. There is no question of estoppel; it is for the protection of the public that the court refuses to enforce such a contract.'

Furthermore, in *Skilton v. Sullivan* (1994) (20.16), the Court of Appeal said that, if the VAT authorities had not already been informed, the court would have been obliged to report to those authorities the fact that one of the parties had dishonestly violated the VAT rules.¹²²

- 20.26** If the contract is illegal, the starting point is that *prima facie* the defendant can raise the defence of illegality to the claimant's action for restitution. Examples where this rule operates satisfactorily are *Parkinson v. College of Ambulance Ltd* (1925),¹²³ where the plaintiff had made a large donation to charity, following the charity's suggestion that it could reciprocate by procuring him a knighthood. His claim to recover on the basis of total failure of consideration was met by the defence of illegality. And, in *Berg v. Sadler & Moore* (1937), the plaintiff used false pretences to buy cigarettes from a tobacco association. He was unable to recover his money from the intended seller.¹²⁴ However, there

119 *McFarlane v. Daniell* (1938) 38 SR (NSW) 337, *per* Jordan CJ.

120 [1999] 2 All ER 429, 433, *per* Colman J, sitting with Sedley LJ; applied in *Pickering v. Deacon* [2003] EWCA Civ 554; *The Times*, 19 April 2003.

121 [1921] 2 KB 716, 729, CA.

122 *The Times*, 25 March 1994 (end of Beldam LJ's judgment).

123 [1925] 2 KB 1, Lush J.

124 [1937] 2 KB 158, CA.

are exceptions to the claimant's inability to obtain restitution under a contract which is invalid for illegality. A party can recover money paid, or obtain recompense in respect of goods or services, where:

- (1) he was ignorant of a fact which caused the transaction to be illegal;¹²⁵ it is not clear whether there is a more general possibility of restitution based on the claimant's innocence; thus, it is uncertain¹²⁶ whether a mere mistake of law (that is, a mistake not induced by the defendant) might now suffice; it has been contended that the Court of Appeal's decision in *Mohamed v. Alaga & Co. (2000)*¹²⁷ might support this, at least where the defendant, a solicitor, is blameworthy in not appreciating that the contract was illegal, and the claimant cannot be expected to have known of a recalcitrant point of illegality; this possibility requires clarification by the courts, but it appears that the law is inclining in this direction; or
- (2) the party seeking restitution belongs to a class of persons intended to be protected by the relevant illegality rule;¹²⁸ or
- (3) the claimant was induced to enter the contract by the defendant's misrepresentation of fact, or fraudulent misrepresentation of law¹²⁹ (which might now extend to misrepresentations of law even if the misrepresentation was innocent),¹³⁰ or
- (4) the claimant has been induced to enter the contract by the defendant's duress;¹³¹ or

125 *Oom v. Bruce* (1810) 12 East 225, 226; 104 ER 87, 88 (insurance for cargo on ship proceeding to England from Russia; at time of contract, plaintiff insured had been unaware that war had recently arisen between these nations; on trading with the enemy, see 20.15).

126 *Hughes v. Liverpool Victoria Friendly Society* [1916] 2 KB 482, CA (fraudulent misrepresentation of law; claimant able to recover premiums on illegal life insurance contract); cf *Harse v. Pearl Life Assurance Co.* [1904] 1 KB 558, CA (innocent misrepresentation of law not entitling claimant to recover premiums on illegal life insurance contract); cf now *Kleinwort Benson Ltd v. Lincoln City Council* [1999] 1 AC 153, HL, abolishing the mistake of law bar to recovery of money paid by error; on the possible impact of this in the context of illegal contracts, see Law Commission, *The Illegality Defence* (Law Commission Consultation Paper No. 189, London, 2009), 2.42.

127 [2000] 1 WLR 190, CA: claimant performing (a) translation and (b) client introduction services for defendant solicitor; element (b) unlawful; whole contract for (a) and (b) invalid for illegality; but claimant awarded a *quantum meruit* in respect of (a); N. Enonchong, [2000] *Restitution Law Review* 241, criticises this decision's reasoning; other decisions have distinguished the *Mohamed* case: see Law Commission, *The Illegality Defence* (Law Commission Consultation Paper No. 189, London, 2009), 4.26 ff, on *Auwad v. Geraghty* [2001] QB 570, 596, CA; and *dicta* in *Dal-Sterling Group v. WSP South West Ltd* [2002] TCLR 20, TCC.

128 *Kiriri Cotton Co. Ltd v. Dewani* [1960] AC 192, 204, PC, *per* Lord Denning (payment of premium by tenant contrary to Ugandan regulations; but statute held to be intended to protect tenants); *Green v. Portsmouth Stadium* [1953] 2 QB 190, CA (bookmaker, at defendant stadium's request, making unlawful payments to stadium; although denied access to stadium, unable to recover payments; statutory invalidity not aimed at protection of bookmakers but of the public at large).

129 As noted at 9.02, citing *Brennan v. Bolt Burdon* [2004] EWCA Civ 1017; [2005] QB 303 (*Treitel* (12th edn, London, 2007), 8-022 ff; J. Cartwright, *Misrepresentation, Mistake and Non-Disclosure* (2nd edn, 2007), 3.20); this decision allows rescission, etc., for misrepresentations of law (following *Kleinwort Benson Ltd v. Lincoln City Council* [1999] 1 AC 153, HL, which abolished the mistake of law bar to recovery of money paid in error); on the possible impact of this in the context of illegal contracts, see Law Commission, *The Illegality Defence* (Law Commission Consultation Paper No. 189, London, 2009), 4.15.

130 See the preceding note on *Kleinwort Benson Ltd v. Lincoln City Council* [1999] 1 AC 153, HL, which abolished the mistake of law bar to recovery of money paid in error.

131 *Smith v. Cuff* (1817) 6 M & S 160, 165; 105 ER 1203, 1205, Lord Ellenborough; *Davies v. London and Provincial Marine Insurance Co.* (1878) 8 Ch D 469, Fry J.

- (5) a final opportunity for restitution arises in the case of certain decisions to resile from an unlawful transaction; the claimant (even though at first conscious of the illegality, and perhaps a main player in it) can obtain restitution if:
- (a) the illegal scheme was voluntarily abandoned by him (that is, he did not abandon it only because he took fright or because he decided to mitigate his position once the illegality had been discovered by authorities or third parties)¹³² and
 - (b) its purpose has not already been fully achieved.¹³³

¹³² *Tribe v. Tribe* [1996] Ch 107, 135, CA, *per* Millett LJ; Law Commission, *The Illegality Defence* (Law Commission Consultation Paper No. 189, London, 2009), 4.52.

¹³³ Law Commission, *The Illegality Defence* (Law Commission Consultation Paper No. 189, London, 2009), 4.45 ff, considering, notably, *Taylor v. Bowers* (1876) 1 QBD 291, CA; *Kearley v. Thomson* (1890) 24 QBD 291, CA; *Bigos v. Boustead* [1951] 1 All ER 92, 97, Pritchard J; *Tribe v. Tribe* [1996] Ch 107, CA.

X

The future

Chapter contents

1. Introduction *para.* 21.01
2. Main differences between the 'soft law' codes and English contract law *para.* 21.02
3. Good faith *para.* 21.03
4. The codification issue *para.* 21.19

21

International and European 'soft law' codes: lessons for English law?

1. INTRODUCTION

21.01 Summary of main points

- (1) Differences between the 'soft law' codes, PECL, the *Principles of European Contract Law*, and UNIDROIT's *Principles of International Commercial Contracts* (2004) and the common law rules will be considered (21.02 and 21.03).
- (2) The civil law notion of 'good faith' (articulated in each of the soft law codes) will be considered (21.03).
- (3) The question whether the common law rules should be codified will be considered (21.25).

There are various 'soft law' codes:

- (1) the global 'commercial' contract code, UNIDROIT's *Principles of International Commercial Contracts*;¹
- (2) PECL, the *Principles of European Contract Law*, drafted by the (Lando) Commission for European Contract Law;²

1 2nd edn, Rome, 2004. M. J. Bonell (University of Rome, 'La Sapienza') has for many years been a leading force within the UNIDROIT organisation and has had a remarkable influence upon this influential work; see also his Bonell, 'Do We Need a Global Commercial Code?' (2000–3) 5 *Uniform Law Review* / *Revue de droit uniforme* 469–81; M. J. Bonell (ed.), *The UNIDROIT Principles in Practice: Case Law and Bibliography on the UNIDROIT Principles of International Commercial Contracts* (2nd edn, Ardsley, NY, 2006); S. Vogenauer and J. Kleinheisterkamp (eds.), *Commentary on the UNIDROIT Principles of International Commercial Contracts* (Oxford, 2009).

2 O. Lando and H. Beale (eds.), *Principles of European Contract Law* (The Hague, 2000); H. G. Collins, *The European Civil Code: The Way Forward* (Cambridge, 2008).

- (3) the ECC, the draft *European Code of Contracts*, drafted by the Academy of European Private Lawyers, under the direction of Giuseppe Gandolfi; and
- (4) DCFR, the *Draft Common Frame of Reference*, prepared by the Study Group on a European Civil Code, and the 'Research Group on EC Private Law' (the 'Acquis Group').

Project (3) is in part a revision of project (2).³ There are lucid summaries of these projects in the essay by Bénédicte Fauvarque-Cosson,⁴ and of projects (1) and (4) by Stefan Vogenauer.⁵ As for (1), Fauvarque-Cosson and Vogenauer note that the UNIDROIT Principles are international, as distinct from (merely) European; and their emphasis is on commercial contracts, and not consumer relations. As for (2), Fauvarque-Cosson notes that the ECC code 'purports less to promote the single market ... It remains faithful to the civil law tradition, in particular to the humanist ideals found in the French tradition.' As for (3), PECL, she comments: 'The "principles", largely inspired by the laws of different Member States, were elaborated by comparing national laws. These are drafted using terms ... so precise and structured that they are more akin to a set of rules ready to be introduced into a Civil Code.' Each project contains rules differing from the common law. None is binding in any State. However, the intellectual and 'transnational' weight of these remarkable projects cannot be ignored. On this, Fauvarque-Cosson comments:⁶ 'In carrying out its mission, European scholarship does not have the pretension of replacing the legislator. At best, it will act as a guide, sometimes to be followed, sometimes disregarded. This form of contribution is one of a series of initiatives which aim to develop a true common legal culture in Europe.'

In the face of this renaissance of European and global private-law scholarship, it would be insular for English lawyers simply to dismiss these projects. But many English lawyers are wary of the English legal system succumbing to harmonisation, and – much worse – having its law modified and distorted by a supranational court having powers to issue a final interpretation (the model, of course, for the European Court of Justice, especially its interpretation of the Jurisdiction Regulation). For example, Lord Hobhouse, a former House of Lords judge, wrote in 1990:⁷ '[I]nternational commerce is best served not by imposing deficient legal

3 *Principles, Definitions and Model Rules of European Private Law Draft Common Frame of Reference*, ed. Christian von Bar and Eric Clive (6 vols., Oxford University Press/Sellier, 2010), prepared by the 'Study Group on a European Civil Code' and the 'Research Group on EC Private Law (Acquis Group)'.

4 B. Fauvarque-Cosson, 'The Contribution of European Jurists in the Field of European Contract Law', in *Liber Amicorum Guido Alpa: National Private Law Systems* (London, 2007), 363, 365; also remarks at J. Cartwright, 'The English Law of Contract: Time for Review?' (2009) 17 *European Review of Private Law* 155, 17–32.

5 S. Vogenauer, 'Common Frame of Reference and UNIDROIT Principles of International Commercial Contracts: Coexistence, Competition, or Overkill of Soft Law?' (2010) 6 *European Review of Contract Law* 143–85.

6 B. Fauvarque-Cosson, 'The Contribution of European Jurists in the Field of European Contract Law', in *Liber Amicorum Guido Alpa: National Private Law Systems* (London, 2007), 363, 368–9.

7 (1990) 106 LQR 530.

schemes upon it but by encouraging the development of the best schemes in a climate of free competition and choice ... What should no longer be tolerated is the unthinking acceptance of a goal of uniformity and its doctrinaire imposition on the commercial community.' An example of the independence of the common law is seen in the (UN) Vienna Convention on Contracts for the International Sale of Goods which has been adopted by many great trading nations: the Convention has *not* replaced the English Sale of Goods Act 1979.

At the other end of the harmonisation spectrum, Hugh Collins has suggested that the eventual achievement of a private law code, including contract law, within Europe will foster a sense of community and citizenship:⁸

If Europe is to progress further in its aims of securing peace and prosperity for its citizens, for the time being it should concentrate not on building controversial supranational sovereign institutions, but rather on helping to support and sustain transnational networks of civil society ... Common rules and principles of private law will provide a superior basis for constructing a transnational civil society ... Development of a civil code, perhaps commencing with contract law, would serve as the next institutional step in creating a system of governance that reinforces the complex aims ... of ever-closer unity whilst respecting the sovereignty of nation States.

He added:⁹

My reasons for believing in the need for a European civil code have little to do with the completion of the internal market, the removal of barriers to cross-border trade, the reduction of transaction costs, or a solution to the perils encountered by frontier workers.

PECL and UNIDROIT's Principles

R. Zimmermann, 'Ius Commune and the Principles of European Contract Law: Contemporary Renewal of an Old Idea', in H. MacQueen and R. Zimmermann (eds.), *European Contract Law: Scots and South African Perspectives* (Edinburgh, 2006), chapter 1

M. J. Bonell, 'Do We Need a Global Commercial Code?' (2000–3) 5 *Uniform Law Review / Revue de droit uniforme* 469–81

8 H. G. Collins, 'Why Europe Needs a Civil Code: European Identity and the Social Model', in *Liber Amicorum Guido Alpa: National Private Law Systems* (London, 2007), 259, 268.

9 *Ibid.*, at 259.

- Lord Mance, 'Is Europe Aiming to Civilise the Common Law?' (Chancery Bar Lecture, Lincoln's Inn, 27 March 2006)
- R. Goode, *Commercial Law in the Next Millennium* (London, 1998) (Hamlyn Lecture Series, 1997) 88–105
- S. Vogenauer, 'Common Frame of Reference and UNIDROIT Principles of International Commercial Contracts: Coexistence, Competition, or Overkill of Soft Law?' (2010) 6 *European Review of Contract Law*, issue 6; and <http://ssrn.com/abstract=1581352>
- S. Whittaker, 'A Framework of Principle for European Contract Law' (2009) 125 LQR 617

Good faith

- R. Brownsword, *Contract Law: Themes for the Twenty-First Century* (2nd edn, Oxford, 2006), chapter 5 (also in R. Brownsword, in M. Furmston (ed.), *The Law of Contract* (3rd edn, London, 2007), chapter 1)
- M. Furmston and G. J. Tolhurst, *Contract Formation: Law and Practice* (Oxford, 2010), chapters 12 and 13 (pre-contractual dealings)
- E. McKendrick, *Contract Law: Text, Cases and Materials* (4th edn, Oxford, 2010), chapter 15
- Lord Steyn, 'Contract Law: Fulfilling the Reasonable Expectations of Honest Men' (1997) 113 LQR 433
- R. Zimmermann and S. Whittaker (eds.), *Good Faith in European Contract Law* (Cambridge, 2000)
- H. MacQueen, 'Good Faith', in H. MacQueen and R. Zimmermann (eds.), *European Contract Law: Scots and South African Perspectives* (Edinburgh, 2006), chapter 2

Codification

- M. Arden, 'Time for an English Commercial Code?' [1997] CLJ 516
- J. Cartwright, 'The English Law of Contract: Time for Review?' (2009) 17 *European Review of Private Law* 155, 168 ff
- R. Goode, 'Removing the Obstacles to Commercial Law Reform' (2007) 123 LQR 602–17
- H. McGregor, *Contract Code: Drawn up on Behalf of the English Law Commission* (Milan, 1993)
- G. H. Treitel, *Some Landmarks of Twentieth Century Contract Law* (Oxford, 2002), 4–9
- A non-English codification of the English rules of contract is available at www.difc.ae/laws-regulations/ (Dubai International Financial Centre).

2. MAIN DIFFERENCES BETWEEN THE 'SOFT LAW' CODES AND ENGLISH CONTRACT LAW

- 21.02 If we confine our attention to UNIDROIT's *Principles of International Commercial Contracts*¹⁰ and to PECL, the *Principles of European Contract Law*,¹¹ the following topics are obvious points of contrast between the approaches adopted in the 'soft law' codes

¹⁰ 2nd edn, Rome, 2004; see M. J. Bonell (ed.), *The UNIDROIT Principles in Practice: Case Law and Bibliography on the UNIDROIT Principles of International Commercial Contracts* (2nd edn, Ardsley, NY, 2006); S. Vogenauer and J. Kleinheisterkamp (eds.), *Commentary on the UNIDROIT Principles of International Commercial Contracts* (Oxford, 2009).

¹¹ O. Lando and H. Beale (eds.), *Principles of European Contract Law* (The Hague, 2000).

and in English law. For reasons of space, it is not possible here to do more than list these points of contrast:

General requirement of good faith

PECL, Article 2:101, UNIDROIT, Article 1.7,¹² and the *Common Frame of Reference*, Article III-1:103,¹³ all adopt this principle as a requirement which operates post-formation. On the position in English law, see 21.03 ff below.

The duty of good faith applies also to pre-contractual negotiations. Thus, PECL, Article 2:301 ('Negotiations Contrary to Good Faith'), states:

- (1) A party is free to negotiate and is not liable for failure to reach an agreement.
- (2) However, a party who has negotiated or broken off negotiations contrary to good faith and fair dealing is liable for the losses caused to the other party.
- (3) It is contrary to good faith and fair dealing, in particular, for a party to enter into or continue negotiations with no real intention of reaching an agreement with the other party.

And UNIDROIT, Article 2.1.15,¹⁴ contains a similar provision.

Firm offers

PECL, Article 2:210(3), and UNIDROIT, Article 2.1.4(2),¹⁵ both provide for irrevocability. On the contrasting position in English law, see 3.35 to 3.37.

Acceptance rules

PECL, Article 2:210(3),¹⁶ and UNIDROIT, Article 2.1.6(2),¹⁷ both provide for acceptance on receipt. On the English postal exception to this approach, see 3.18 to 3.28; and, for

12 M. J. Bonell (ed.), *The UNIDROIT Principles in Practice: Case Law and Bibliography on the UNIDROIT Principles of International Commercial Contracts* (2nd edn, Ardsley, NY, 2006), 83 ff; S. Vogenauer and J. Kleinheisterkamp (eds.), *Commentary on the UNIDROIT Principles of International Commercial Contracts* (Oxford, 2009), 165 ff.

13 *Principles, Definitions and Model Rules of European Private Law Draft Common Frame of Reference*, ed. Christian von Bar and Eric Clive (6 vols., Oxford University Press/Sellier, 2010), prepared by the 'Study Group on a European Civil Code' and the 'Research Group on EC Private Law (Acquis Group)'.

14 M. J. Bonell (ed.), *The UNIDROIT Principles in Practice: Case Law and Bibliography on the UNIDROIT Principles of International Commercial Contracts* (2nd edn, Ardsley, NY, 2006), 138 ff; S. Vogenauer and J. Kleinheisterkamp (eds.), *Commentary on the UNIDROIT Principles of International Commercial Contracts* (Oxford, 2009), 299 ff.

15 M. J. Bonell (ed.), *The UNIDROIT Principles in Practice: Case Law and Bibliography on the UNIDROIT Principles of International Commercial Contracts* (2nd edn, Ardsley, NY, 2006), 13 ff; S. Vogenauer and J. Kleinheisterkamp (eds.), *Commentary on the UNIDROIT Principles of International Commercial Contracts* (Oxford, 2009), 245 ff.

16 G. Quinot, in H. MacQueen and R. Zimmermann (eds.), *European Contract Law: Scots and South African Perspectives* (Edinburgh, 2006), chapter 3.

17 M. J. Bonell (ed.), *The UNIDROIT Principles in Practice: Case Law and Bibliography on the UNIDROIT Principles of International Commercial Contracts* (2nd edn, Ardsley, NY, 2006), 83 ff; S. Vogenauer

partial adoption of that rule, protecting the offeree against revocation if posting of the acceptance precedes notification of revocation, see PECL, Article 2:202(1), and UNIDROIT, Article 2.1.4(1).¹⁸

Battle of the forms

PECL, Article 2:209, states that ‘general conditions form part of the contract to the extent that they are common in substance’;¹⁹ and UNIDROIT, Article 2.1.22,²⁰ states that ‘a contract is concluded on the basis of the agreed terms and of any standard terms which are common in substance unless one party clearly indicates in advance, or later and without undue delay informs the other party, that it does not intend to be bound by such a contract’. On the contrasting position in English law, adopting instead the ‘last shot’ or ‘mirror image’ analysis, see 3.32 to 3.34.

Absence of a doctrine of consideration for the formation or modification of contracts

Neither PECL, Article 2:101(1), nor UNIDROIT (see below) requires such an element: it is enough that the contract or agreed modification was intended to create legal relations, and that the agreement is otherwise not vitiated by reason of coercion, etc., and that it is not unlawful.

Thus PECL, Article 2:101(1) (‘Conditions for the Conclusion of a Contract’) states:

A contract is concluded if: the parties intend to be legally bound, and they reach a sufficient agreement without any further requirement.

UNIDROIT, Articles 1.3 and 3.2, make no reference to the common law requirement of a deed or consideration, but the commentaries explicitly reject these requirements.²¹

On the English general requirement of consideration for both the formation and the modification of a contract, see chapter 5; but, for comment on the loosening of this ‘consideration’ requirement for both increasing pacts (more money for the same task) and decreasing pacts (reduction in the price payable or in the level of performance owed) in the context of contractual modification, see 5.33 to 5.35, 5.43 and 5.63. On the English rules governing deeds (or ‘covenants’), see 5.03 ff.

and J. Kleinheisterkamp (eds.), *Commentary on the UNIDROIT Principles of International Commercial Contracts* (Oxford, 2009), 165 ff.

18 M. J. Bonell (ed.), *The UNIDROIT Principles in Practice: Case Law and Bibliography on the UNIDROIT Principles of International Commercial Contracts* (2nd edn, Ardsley, NY, 2006), 113.

19 A. D. M. Forte, in H. MacQueen and R. Zimmermann (eds.), *European Contract Law: Scots and South African Perspectives* (Edinburgh, 2006), chapter 4.

20 M. J. Bonell (ed.), *The UNIDROIT Principles in Practice: Case Law and Bibliography on the UNIDROIT Principles of International Commercial Contracts* (2nd edn, Ardsley, NY, 2006), 156 ff; S. Vogenauer and J. Kleinheisterkamp (eds.), *Commentary on the UNIDROIT Principles of International Commercial Contracts* (Oxford, 2009), 341 ff.

21 M. J. Bonell (ed.), *The UNIDROIT Principles in Practice: Case Law and Bibliography on the UNIDROIT Principles of International Commercial Contracts* (2nd edn, Ardsley, NY, 2006), 73–4, 189–90; S. Vogenauer and J. Kleinheisterkamp (eds.), *Commentary on the UNIDROIT Principles of International Commercial Contracts* (Oxford, 2009), 125–7, 404–7.

Mistake

In *'The Great Peace'* (2002) (10.08, 10.12 ff), the Court of Appeal rejected (not entirely uncontroversially) a doctrine of equitable shared mistake concerning the nature of the subject matter. That boldly negative decision has left isolated the common law concept of shared mistake rendering the supposed transaction *void* (10.06 ff). This can be contrasted with the schemes of both PECL and UNIDROIT, where:

- (1) 'initial impossibility' is expressly stated not to be a ground of invalidity (PECL, Article 4:102; UNIDROIT,²² Article 3.3) (contrast on this point English law, where the contract will be void: 10.06 ff); and
- (2) shared serious error can only render the contract *voidable*: (PECL, Articles 4:103, 4:112 to 4:116; UNIDROIT,²³ Articles 3.4, 3.5, 3.12 to 3.18).

Supervening difficulty

For a full citation of the 'soft law' provisions on this, see 16.09.

PECL, Article 6:111, states:

- (2) If ... performance of the contract becomes excessively onerous because of a change of circumstances, the parties are bound to enter into negotiations with a view to adapting the contract or terminating it ...

In default of such agreement, there is provision for judicial termination or revision.

UNIDROIT, Articles 6.2.2 and 6.2.3,²⁴ permit renegotiation or, in default of agreement, judicial termination or revision, in respect of 'the occurrence of events fundamentally [altering] the equilibrium of the contract', provided the matter is not covered by the risk of the contract.

On the contrasting position in English law, adopting a restrictive approach to pleas of 'frustration', see 16.09.

Interpretation

For the English rules restricting evidence concerning the parties' negotiations or subsequent conduct, see 14.13 ff; and for Eric Clive's perceptive remarks on the functional

22 M. J. Bonell (ed.), *The UNIDROIT Principles in Practice: Case Law and Bibliography on the UNIDROIT Principles of International Commercial Contracts* (2nd edn, Ardsley, NY, 2006), 191 ff; S. Vogenauer and J. Kleinheisterkamp (eds.), *Commentary on the UNIDROIT Principles of International Commercial Contracts* (Oxford, 2009), 408 ff.

23 M. J. Bonell (ed.), *The UNIDROIT Principles in Practice: Case Law and Bibliography on the UNIDROIT Principles of International Commercial Contracts* (2nd edn, Ardsley, NY, 2006), 193 ff; S. Vogenauer and J. Kleinheisterkamp (eds.), *Commentary on the UNIDROIT Principles of International Commercial Contracts* (Oxford, 2009), 411 ff.

24 M. J. Bonell (ed.), *The UNIDROIT Principles in Practice: Case Law and Bibliography on the UNIDROIT Principles of International Commercial Contracts* (2nd edn, Ardsley, NY, 2006), 327 ff; S. Vogenauer and J. Kleinheisterkamp (eds.), *Commentary on the UNIDROIT Principles of International Commercial Contracts* (Oxford, 2009), 717 ff.

similarity of the English combination of interpretation and rectification doctrines *in the same litigation*, see 14.16.

PECL, Article 5:101 ('General Rules of Interpretation') states:²⁵

(1) A contract is to be interpreted according to the common intention of the parties even if this differs from the literal meaning of the words.

(2) If it is established that one party intended the contract to have a particular meaning, and at the time of the conclusion of the contract the other party could not have been unaware of the first party's intention, the contract is to be interpreted in the way intended by the first party.

(3) If an intention cannot be established according to (1) or (2), the contract is to be interpreted according to the meaning that reasonable persons of the same kind as the parties would give to it in the same circumstances.

And PECL, Article 5:102 ('Relevant Circumstances'), states:

In interpreting the contract, regard shall be had, in particular, to:

- (a) the circumstances in which it was concluded, including the preliminary negotiations;
- (b) the conduct of the parties, even subsequent to the conclusion of the contract;
- (c) the nature and purpose of the contract;
- (d) the interpretation which has already been given to similar clauses by the parties and the practices they have established between themselves;
- (e) the meaning commonly given to terms and expressions in the branch of activity concerned and the interpretation similar clauses may already have received;
- (f) usages; and
- (g) good faith and fair dealing.

UNIDROIT, Article 4.3, permits a similarly wide range of matters to be taken into account.

Assurance of performance

See PECL, Article 8:105 (17.14);²⁶ UNIDROIT, Article 7.3.4,²⁷ contains a similar provision.

25 E. Clive, in H. MacQueen and R. Zimmermann (eds.), *European Contract Law: Scots and South African Perspectives* (Edinburgh, 2006), chapter 7.

26 T. Naudé, in H. MacQueen and R. Zimmermann (eds.), *European Contract Law: Scots and South African Perspectives* (Edinburgh, 2006), chapter 11.

27 M. J. Bonell (ed.), *The UNIDROIT Principles in Practice: Case Law and Bibliography on the UNIDROIT Principles of International Commercial Contracts* (2nd edn, Ardsley, NY, 2006), 385 ff; S. Vogenauer and J. Kleinheisterkamp (eds.), *Commentary on the UNIDROIT Principles of International Commercial Contracts* (Oxford, 2009), 849 ff.

Specific performance

For the English approach, confining this remedy in practice to agreements for the transfer of interests in land or shares in *private* companies or 'unique' chattels, and to precise and easily supervised tasks not involving 'personal services' by individuals (as distinct from companies), see 18.14 to 18.19.

PECL, Article 9:102 ('Non-Monetary Obligations'), states:²⁸

(1) The aggrieved party is entitled to specific performance of an obligation other than one to pay money, including the remedying of a defective performance.

(2) Specific performance cannot, however, be obtained where:

- (a) performance would be unlawful or impossible; or
- (b) performance would cause the debtor unreasonable effort or expense; or
- (c) the performance consists in the provision of services or work of a personal character or depends upon a personal relationship, or
- (d) the aggrieved party may reasonably obtain performance from another source.

(3) The aggrieved party will lose the right to specific performance if it fails to seek it within a reasonable time after it has or ought to have become aware of the non-performance.

UNIDROIT, Article 7.2.2,²⁹ contains a similar provision.

Damages and the defence of contributory negligence

Contributory negligence is contemplated even in respect of the primary wrongdoer's breach of a strict obligation in PECL, Article 9:504, and UNIDROIT, Article 7.4.7.³⁰ This contrasts with the position in English law, as explained at 18.50.

Remoteness of damage

The English test is considered in detail at 18.40 ff. It is instructive to compare the formulations of the remoteness test contained in PECL, Article 9:503,³¹ UNIDROIT, Article 7.4.4,³² and the Vienna Convention on the International Sale of Goods (not ratified by the UK).

28 S. Eiselen, in H. MacQueen and R. Zimmermann (eds.), *European Contract Law: Scots and South African Perspectives* (Edinburgh, 2006), chapter 10.

29 M. J. Bonell (ed.), *The UNIDROIT Principles in Practice: Case Law and Bibliography on the UNIDROIT Principles of International Commercial Contracts* (2nd edn, Ardsley, NY, 2006), 364 ff; S. Vogenauer and J. Kleinheisterkamp (eds.), *Commentary on the UNIDROIT Principles of International Commercial Contracts* (Oxford, 2009), 784 ff.

30 M. J. Bonell (ed.), *The UNIDROIT Principles in Practice: Case Law and Bibliography on the UNIDROIT Principles of International Commercial Contracts* (2nd edn, Ardsley, NY, 2006), 410–12 and 897–900.

31 S. Eiselen, in H. MacQueen and R. Zimmermann (eds.), *European Contract Law: Scots and South African Perspectives* (Edinburgh, 2006), chapter 10, at 270 ff.

32 2nd edn, Rome, 2004; see M. J. Bonell (ed.), *The UNIDROIT Principles in Practice: Case Law and Bibliography on the UNIDROIT Principles of International Commercial Contracts* (2nd edn, Ardsley, NY,

PECL, Article 9:503 ('Foreseeability') states:

The non-performing party is liable only for loss which it foresaw or could reasonably have foreseen at the time of conclusion of the contract as a likely result of its non-performance, unless the non-performance was intentional or grossly negligent.

UNIDROIT, Article 7.4.4 ('Foreseeability of Harm'), states:

The non-performing party is liable only for harm which it foresaw or could reasonably have foreseen at the time of the conclusion [viz formation] of the contract as being likely to result from its non-performance.

And the Vienna Convention on the International Sale of Goods, Article 74, states:

Such damages may not exceed the loss which the party in breach foresaw or ought to have foreseen at the time of the conclusion of the contract, in the light of the facts and matters of which he then knew or ought to have known, as a possible consequence of the breach of contract.

The following comparative remarks on these three provisions may be made:

- (1) *Lower level of foresight than in England.* All three non-English tests cited above seem to be calibrated slightly more generously than English law in favour of the innocent party: the UNIDROIT and PECL tests refer to harm which is 'likely' to result; the Vienna Convention test refers to harm which is a 'possible' consequence: as noted at 18.42, in English law the 'serious possibility' test is the preferred formulation,³³ and is approved by Burrows.³⁴
- (2) *Assessed at time of formation.* However, the three non-English tests also unite in applying the test of foreseeability at the time of the contract's formation, rather than its breach; and this is also the English approach (18.42).
- (3) *Foresight rather than contemplation.* Furthermore, the three non-English tests use the language of 'foresight' rather than 'contemplation'. The latter term seems preferable in England because 'foresight' or 'foreseeability' invites confusion between the contractual test and the more claimant-friendly remoteness test for negligence (18.42): a local problem, perhaps.
- (4) *Defendant's foresight rather than joint contemplation.* All three non-English tests adopt the perspective of the party in breach, finding it unnecessary to refer to the other party's contemplation or foresight.³⁵ This contrasts with the bilateral focus of

2006), 404–5; S. Vogenauer and J. Kleinheisterkamp (eds.), *Commentary on the UNIDROIT Principles of International Commercial Contracts* (Oxford, 2009), 885 ff.

33 Lord Walker in the *Transfield* case, [2008] UKHL 48; [2009] 1 AC 61, at [76] noting '*The Heron II*' [1969] 1 AC 350, 400, 415 and 425.

34 A. S. Burrows, *Remedies for Torts and Breach of Contract* (3rd edn, Oxford, 2004), 88, 94.

35 S. Eiselen, in H. MacQueen and R. Zimmermann (eds.), *European Contract Law: Scots and South African Perspectives* (Edinburgh, 2006), chapter 10, at 277, commending this one-sided inquiry.

the English approach, considering both parties' contemplation (although not much (if anything) seems to turn on this point in practice: see 18.43 case (1), *Hadley v. Baxendale*, where Baron Alderson referred to the 'contemplation of both parties', at least for the purpose of limb 2 (special information)).

- (5) *Ordinary course of things and special circumstances*. Only the Vienna Convention echoes Baron Alderson's distinction in *Hadley v. Baxendale* (18.43 case (1)) between contemplation of harm occurring in the ordinary course of things and special contemplation in light of particular information.
- (6) *Type and extent of losses*. As noted at 18.42, the *Wagon Mound* test in the tort of negligence allows recovery if the *head of loss* was reasonably foreseeable, even if the *extent of the loss* was not foreseeable. Whereas, in the case of contractual claims for *lost profits*, a distinction has been made, and remains important, between ordinary loss of profits, and loss of exceptional profits, that is, a distinction between *degrees of loss* under the same broad head of lost profits: see the *Victoria Laundry* case (1949) (18.43 case (2)) (extent of profits matters) and *Parsons v. Uttley Ingram* (1978) (18.43 case (4)) (extent of physical damage does not matter). The Official Commentary on the UNIDROIT principle acknowledges the distinction drawn in English law between the type, or head, of loss and its extent, but then adds '... unless the extent is such as to transform the harm into one of a different kind'.³⁶
- (7) *Remoteness and scope of duty*. The three tests cited here are (mercifully) free from the tangle now besetting English law, following the introduction of an overlapping test of 'scope of duty': see the discussion of the *Transfield* case (2008) at 18.43 and 18.45 to 18.47.
- (8) *Heinous breach*. Only PECL, and not UNIDROIT or the Vienna Convention, adopts an 'all the consequences of breach' sub-rule for a breach which is grossly negligent or intentional. English law does not make this distinction for the purpose of *breach of contract*, although the 'all the consequences' test is applicable to actions in tort for deceit: on the *Smith New Court* test, see 9.12.

3. GOOD FAITH

21.03 This topic has produced a vast literature.³⁷ This concept can apply both in the performance of contracts and, at the pre-contractual phase, the same concept can be used

36 M. J. Bonell (ed.), *The UNIDROIT Principles in Practice: Case Law and Bibliography on the UNIDROIT Principles of International Commercial Contracts* (2nd edn, Ardsley, NY, 2006), 404.

37 J. Beatson and D. Friedmann (eds.), *Good Faith and Fault in Contract Law* (Oxford, 1995), chapter 2 (N. Cohen, Israel), chapter 6 (E. A. Farnsworth, USA) and chapter 7 (W. Ebke and B. M. Steinhauer, Germany); A. Berg, (2003) 119 LQR 357; R. Brownsword, *Contract Law: Themes for the Twenty-First Century* (2nd edn, Oxford, 2006), chapter 5 (also in R. Brownsword, in M. Furmston (ed.), *The Law of Contract* (3rd edn, London, 2007), chapter 1); S. G. Burton and E. G. Andersen, *Contractual Good Faith* (Boston, 1995); M. Clarke, (1993) 23 HKLJ 318; H. G. Collins, (1994) 14 OJLS 229; H. G. Collins, *The Law of Contract* (4th edn, Cambridge, 2003), chapters 10 and 15; A. Forte (ed.), *Good Faith in Contract and Property Law* (Oxford, 1999); M. Furmston and G. J. Tolhurst, *Contract Formation: Law and Practice* (Oxford, 2010), chapters 12 and 13 (pre-contractual dealings); O. Lando, 'Is Good Faith an Overarching General Clause in the Principles of European Contract Law?', in *Liber Amicorum Guido Alpa: National Private Law Systems* (London, 2007), 601; E. McKendrick, 'The Meaning of Good Faith', in *Liber Amicorum Guido*

to control the parties' capacity to withdraw from pre-contractual negotiations. 'Good faith' in the performance of contracts is a prominent feature of civil law systems of contract law (section 242 of the German *Bürgerliches Gesetzbuch* (BGB); Article 1134 of the French Civil Code; Articles 1337, 1366 and 1375 of the Italian Civil Code); and the same concept has been adopted in the USA, both in the *Restatement of the Law Second, Contracts* (1981, section 205) and the Uniform Commercial Code (section 1-203); furthermore, UNIDROIT's *Principles of International Commercial Contracts* (2004), Article 1.7,³⁸ the Principles of European Contract Law, Article 2:201, and the Common Frame of Reference, Article III-1:103,³⁹ adopt this principle. As for the definition of good faith, McKendrick notes:⁴⁰ 'There is a spectrum of possible meanings ... At the one end of the spectrum good faith means no more than honesty ... At the other end of the spectrum good faith may require [a party] ... to give priority to the best interests of the other party', as in the manner of a fiduciary. And he adds: '[A] court is more likely to find that a party has broken a good faith obligation when it has acted in bad faith; that is to say, it has acted contrary to its own interests with the aim or intent of inflicting injury on the other party to the contract.'

- 21.04 But 'good faith' is not an explicitly recognised general doctrine in English contract law⁴¹ (however, see 21.06 to 21.09 for specific judicial and statutory contexts where good faith is recognised or immanent). As Bingham LJ said in *Interfoto Picture Library Ltd v. Stiletto Visual Programmes Ltd* (1989):⁴²

In many civil law systems ... the law of obligations recognises and enforces an overriding principle that in making and carrying out contracts parties should act in good faith ... [Its] effect is perhaps most aptly conveyed by such metaphorical colloquialisms as 'playing fair', 'coming clean'. It is in essence a principle of fair and open dealing ... English law has, characteristically, committed itself to no such overriding

Alpa: National Private Law Systems (London, 2007), 687; E. McKendrick, *Contract Law: Text, Cases and Materials* (4th edn, Oxford, 2010), chapter 15; H. MacQueen, 'Good Faith, Mixed Legal Systems and the Principles of European Contract Law', in *Liber Amicorum Guido Alpa: National Private Law Systems* (London, 2007), 614; J. O'Connor, *Good Faith in English Law* (Aldershot, 1990), chapter 3; Lord Steyn, 'Contract Law: Fulfilling the Reasonable Expectations of Honest Men' (1997) 113 LQR 433; G. Teubner, (1998) 61 MLR 11; R. Zimmermann and S. Whittaker (eds.), *Good Faith in European Contract Law* (Cambridge, 2000) (reviewed, N. Andrews (2001) *Civil Justice Quarterly* 197); H. MacQueen and R. Zimmermann (eds.), *European Contract Law: Scots and South African Perspectives* (Edinburgh, 2006), 17–18 (Zimmermann), and chapter 2 (MacQueen).

- 38 M. J. Bonell (ed.), *The UNIDROIT Principles in Practice: Case Law and Bibliography on the UNIDROIT Principles of International Commercial Contracts* (2nd edn, Ardsley, NY, 2006), 83 ff; S. Vogenauer and J. Kleinheisterkamp (eds.), *Commentary on the UNIDROIT Principles of International Commercial Contracts* (Oxford, 2009), 165 ff.
- 39 *Principles, Definitions and Model Rules of European Private Law Draft Common Frame of Reference*, ed. Christian von Bar and Eric Clive (6 vols., Oxford University Press/Sellier, 2010), prepared by the 'Study Group on a European Civil Code' and the 'Research Group on EC Private Law (Acquis Group)'.
- 40 E. McKendrick, 'The Meaning of Good Faith', in *Liber Amicorum Guido Alpa: National Private Law Systems* (London, 2007), 687, 692, 696.
- 41 E. McKendrick, *Contract Law: Text, Cases and Materials* (4th edn, Oxford, 2010), chapter 15 (examining R. Brownsword's sophisticated discussion in M. Furmston (ed.), *The Law of Contract* (3rd edn, London, 2007), 1.79 ff).
- 42 [1989] QB 433, 439, CA.

principle but has developed piecemeal solutions in response to demonstrated problems of unfairness.

21.05 The argument here will be that (1) in English law the principle of good faith is not at all required in the context of *pre-contractual negotiations* because of the highly developed and fertile array of existing doctrines; and (2) as for articulating in English law the concept of 'good faith' as a general principle governing *performance of contracts*, the case is more evenly balanced; however, there would be only a slight benefit in making such a change; there would be a problem for practitioners adjusting to the new concept; but the courts would be unlikely to use the concept dynamically. In short, good faith as a general norm regulating performance of contracts might become an empty affirmation of the pervasive sensitivity of common law and equity to problems of fair dealing; and it would add little, if anything. And so, at 21.20, my conclusion will be: the inevitable anxiety and uncertainty experienced within the legal profession when advising their clients might in fact outweigh the possible and marginal benefits of such a change.

21.06 In fact, there are many English doctrines where the courts have arguably acted on a principle of good faith or fair dealing when introducing, shaping and applying a particular doctrine. Ten such *judicial* instances will now be listed (see 21.07 ff for statutory examples):

- (1) *The doctrine of promissory estoppel and waiver and estoppel at common law* (5.53 to 5.63).
- (2) *Unconscionable advantage*. Rescission or rectification where one party has unconscionably acquiesced in the other's mistake, and the 'snapping-up' cases decided at common law (3.65).
- (3) *Vitiating factors*. Grounds of vitiation based upon coercion, undue influence, or exploitation (chapter 11).
- (4) *Specific duties to disclose* (9.34).
- (5) *Fiduciary duties*. The duties of fair dealing imposed on agents and other fiduciaries when they contract with their principals, beneficiaries or other protected persons.⁴³
- (6) *Mediation agreements*. Recognition of dispute-resolution agreements which require the parties at least to proceed to mediation (*Cable & Wireless plc v. IBM United Kingdom Ltd* (2002): 2.13).
- (7) *Implied terms*. Notably, the recent (slightly qualified) insertion of duties to act not wholly unreasonably when unilaterally revising terms in finance agreements (*Paragon Finance plc v. Nash* (2002): 13.20) and the recent *dictum* in the *Berkeley Community Villages Ltd v. Pullen* (2007) case (21.13 at (6) below); and the Privy Council in *Pratt Contractors Ltd v. Transit New Zealand* (2003) (3.51) has acknowledged that there

43 *Calvert v. William Hill Credit Ltd* [2008] EWCA Civ 1427; [2009] Ch 330, at [53]; *Parker and Mellows: The Modern Law of Trusts* (9th edn, London, 2008), 10-048 ff; J. Edelman, 'When Do Fiduciary Duties Arise?' (2010) 126 LQR 302.

is an implied duty on the part of the invitor to conduct the tender process in good faith.⁴⁴

- (8) *The penalty jurisdiction* (19.03).
- (9) *Equitable relief against forfeiture of proprietary or possessory interests* (17.39).
- (10) *Right to terminate is wholly disproportionate or severe*. Decisions denying that a party has a right to terminate a contract where this would be a wholly disproportionate or severe response to the relevant breach (both '*The Hansa Nord*' (1976) (17.37) and *Rice v. Great Yarmouth Borough Council* (2000) (17.25) exemplify this).

21.07 There are also statutory examples. First, the Unfair Terms in Consumer Contracts Regulations 1999 (15.33) contain 'good faith' as one of the criteria for determining the validity of a standard clause in a contract for supply of goods or services affecting a consumer. In the House of Lords' decision in *Director-General of Fair Trading v. First National Bank* (2002),⁴⁵ Lord Bingham said⁴⁶ that this imported a requirement of fair and open dealing, and that openness required clarity and 'no pitfalls'.

He added that fair dealing requires that the supplier should not, deliberately or otherwise, take advantage of the consumer's necessity, indigence, lack of experience, unfamiliarity, or weak bargaining position. Lord Bingham recalled that the great eighteenth-century judge, Lord Mansfield, had been a champion of 'good faith' in the insurance context.⁴⁷

Lord Steyn in *Director-General of Fair Trading v. First National Bank* (2002)⁴⁸ rejected the view that good faith in the 1999 Regulations should be limited to 'procedural' shortcomings, as distinct from a broader notion of unfairness.

21.08 Secondly, the Misrepresentation Act 1967 gives the courts a discretion to refuse rescission of a contract (or reverse self-help rescission) for non-fraudulent misrepresentations (9.21),⁴⁹ and this permits a broad consideration of fairness.

21.09 Another example is section 15A of the Sale of Goods Act 1979 (17.35). This prevents termination for breach of implied terms where the buyer is a non-consumer and the relevant breach is trivial. It is designed to temper the perceived harshness of the common law's approach to the rejection of goods on technical (and bad faith) grounds, when the relevant defect does not cause the buyer any real loss or problem.

21.10 *Blots on the law?* Admittedly, there are three striking examples of decisions which appear to be an affront to any notion of good faith: *Arcos v. Ronaasen* (1933) (17.36), *Union Eagle Ltd v. Golden Achievement Ltd* (1997) (17.40) and *White & Carter v. McGregor* (1962) (18.05). But each of these decisions might be defended. First, the *Arcos* case (1933)

44 [2003] UKPC 83; [2004] BLR 143; 100 Con LR 29.

45 [2002] 1 AC 481; [2001] UKHL 52.

46 *Ibid.*, at [17].

47 An allusion to, notably, *Carter v. Boehm* (1766) 3 Burr 1905.

48 [2001] UKHL 52; [2002] 1 AC 481, at [36].

49 Section 2(2) of the Misrepresentation Act 1967.

(17.36) is not as outlandish as might at first appear: the discrepancy in the width of the timber supplied was not microscopic (although this made no difference to the buyer, it seems; but he might have changed his mind and either wished to use the wood for a new purpose where the difference might matter, or he might have decided to try to sell the timber, when its exact specification might again have mattered). Secondly, the buyer's ten-minute delay in paying for the real property in the *Union Eagle* case (1997) (17.40) might have made a difference if there were dependent transactions. Furthermore, as Lord Hoffmann persuasively suggested in this case, there is a need for a very bright line indeed in commercial conveyancing transactions. Finally, the *White & Carter* (1962) problem (see further 18.05) is a classic dilemma which divided the House of Lords three to two, and subsequent decisions (18.09 ff) have mostly favoured the innocent party's right to maintain the contract.

- 21.11 *Pre-contractual express agreements to negotiate in good faith.* The law is summarised at 2.06. The main proposition is that English law does not recognise as valid an agreement to negotiate in good faith or reasonably the terms of the main contract. In the leading case, *Walford v. Miles* (1992)⁵⁰ (2.07), the House of Lords held that an agreement to negotiate in good faith or reasonably is uncertain and void. The two main reasons for this are: bargaining in good faith (or reasonably) is too vague; and the courts would become embroiled in complicated inquiries into the reasons why negotiations broke down. It is submitted that *Walford v. Miles* (1992) (2.07) is sound: an express agreement to negotiate *towards the main contract* should remain void for uncertainty.
- 21.12 *Pre-contractual negotiations: time to impose a general duty of good faith?* Nor should English law adopt a general principle of good faith in the pre-contractual context. The existing miscellany of doctrines adequately serves (proprietary estoppel, restitution, tortious liability for certain types of misrepresentation, implied collateral warranties, as in *Blackpool and Fylde Aero Club v. Blackpool Borough Council* (1990) (3.50)). As Collins aptly observes, English law is exacting in this sphere, requiring even a positive obligation to respect certain expectations engendered by the parties' pre-contractual dealings.⁵¹ The context is complex and varied. Different contexts receive different legal treatments. By contrast, Berg's list of 'good faith obligations' (2.09), which he offers as a rejoinder to *Walford v. Miles* (1992) (2.07), would provide much material for litigation where large deals break down. Berg proposes Utopian standards of fair dealing: that each negotiating party should 'have an open mind' and 'a willingness to consider' the other side's proposals; there should be 'an obligation not to take advantage' of the other side's ignorance; and there should be a duty 'not to withdraw giving as the cause something which ... is extremely unreasonable'.⁵² It is not clear that even a convocation of bishops would wish to subject themselves to this demanding set of criteria.

50 [1992] 2 AC 128, HL.

51 H. G. Collins, *The Law of Contract* (4th edn, Cambridge, 2003), chapter 10.

52 A. Berg, (2003) 119 LQR 357, 363.

21.13 *Post-formation implied duty to perform in good faith.* This leaves the question whether the English courts should recognise a general duty to perform a contract in good faith. Brownsword has set out the arguments for and against introducing such a duty.⁵³ The arguments for can be summarised as:

- (1) good faith can be dealt with by the courts in a 'clean and direct fashion', 'coherently and effectively';
- (2) such recognition would ensure that the law reflects 'reasonable expectations'; and
- (3) its recognition as an explicit and general doctrine will foster a 'culture of trust and co-operation'.

The arguments against are:

- (1) 'English contract law is premised on adversarial self-interested dealing';
- (2) 'good faith' is too vague an idea; its implementation would require 'difficult inquiries into contracting parties' reasons'; and
- (3) it would be inappropriate in contexts where the parties' dealings 'openly tolerate opportunism'.

21.14 Post-formation 'good faith', in Lord Steyn's view, would be an unobjectionable formula for a norm which reflects commercial practice or the values of the market-place.⁵⁴ And, as he commented judicially in *First Energy (UK) Ltd v. Hungarian International Bank Ltd* (1993):⁵⁵

[T]he reasonable expectations of honest men must be protected ... It is the objective which has been and still is the principal moulding force of our law of contract ... [If] the *prima facie* solution to a problem runs counter to [this], this criterion requires a rigorous re-examination of the problem to ascertain whether the law does indeed compel demonstrable unfairness.

21.15 However, when one considers the range and pliability of English doctrines already embodying a notion of good faith or fair dealing, it seems unlikely that many cases will be differently decided if 'good faith' were explicitly introduced as a general principle.

21.16 It is necessary to consider another objection: that good faith's adoption as a general feature of contract law might unsettle existing rules and provoke a spate of litigation in which established doctrine would need to be re-examined through the new prism. A period of uncertainty would be unwelcome. And it would be unlikely to engender any significant change. For the English courts are unlikely to change their spots. The values of commercial certainty and predictability, and the need to keep the law rooted in the

53 R. Brownsword, in M. Furmston (ed.), *The Law of Contract* (3rd edn, London, 2007), 1.81 ff.

54 Lord Steyn, 'Contract Law: Fulfilling the Reasonable Expectations of Honest Men' (1997) 113 LQR 433.

55 [1993] 2 Lloyd's Rep 194, 196, CA.

ordinary or reasonable expectations of businesses and consumers, would have a dampening effect upon this principle. For example, English courts would surely not use the explicit concept of good faith to reverse the settled doctrine that a prospective party is not obliged to point out the other side's misapprehension concerning the nature of the proposed subject matter.⁵⁶

- 21.17 However, it would be a different matter if the English law of contract were to be placed in the hands of a supra-national court. The English system would then have lost control. Instead, the concept would be applied and developed, perhaps aggressively, by outsiders not attuned to the tradition of the common law, its peculiar methods, and its hallowed values.
- 21.18 In short, 'good faith', entrusted solely to English judges, and confined to performance of contracts, is unlikely to unsettle the array of common law doctrines and rules which have evolved over centuries. The inevitable anxiety and uncertainty experienced within the legal profession when advising their clients would outweigh the speculative and marginal benefits of such a change.

4. THE CODIFICATION ISSUE

- 21.19 *Nature and benefits of a code.*⁵⁷ A code is composed of a set of legislative provisions. It is normally quite systematic and relatively succinct (although the text might be amplified by comments and illustrations, as in the case of the American Law Institute's Restatements) (see also Hugh Collins' visionary perspective on the merits of an European Code of Private Law, at 21.01). There is no doubt that compiling a code would be an occasion for spring-cleaning, perhaps even for major innovation. Lumber could be jettisoned. A code would be up to date (however fleetingly) and portable.⁵⁸ Of course, in the age of the Internet and

⁵⁶ *Smith v. Hughes* (1871) LR 6 QB 597; *Bell v. Lever Bros Ltd* [1932] AC 161, 224, HL; *BCCI v. Ali* [2002] 1 AC 251, HL, at [72], on which see 3.66 ff.

⁵⁷ M. Arden, [1997] CLJ 516; H. G. Collins, 'Why Europe Needs a Civil Code', in *Liber Amicorum Guido Alpa: National Private Law Systems* (London, 2007), 259; H. G. Collins, *The European Civil Code: The Way Forward* (Cambridge, 2008); R. Goode, 'Removing the Obstacles to Commercial Law Reform' (2007) 123 LQR 602–17; Lord Falconer, speech, www.dca.gov.uk/speeches/2005/lc150905.htm; A. Hartkamp and C. Joustra (eds.), *Towards a European Civil Code* (3rd edn, Nijmegen, 2004); H. Kronke, (2005) *Loyola of Los Angeles Law Review* 287–99; O. Lando, *Principles of European Contract Law and UNIDROIT Principles: Similarities, Differences and Perspectives* (Rome, 2002); Lord Mance, 'Is Europe Aiming to Civilise the Common Law?' (Chancery Bar Lecture, Lincoln's Inn, 27 March 2006); S. Vogenauer (ed.), *The Harmonisation of European Contract Law* (Oxford, 2005); Clifford Chance Survey on European Contract Law (Clifford Chance, April 2005); 'European Contract Law: The Way Forward?', House of Lords Select Committee (EU committee), House of Lords Paper 95 (2005), www.publications.parliament.uk/pa/ld200405/ldselect/ldcom/95/9502.htm; N. Andrews, 'Le droit anglais: a-t-il besoin d'un code?', in *Essays in Honour of Konstantinos D. Kerameus* (Athens and Brussels, 2009), 19–26. A recent codification of the common law rules of contract is available at www.difc.ae/laws-regulations/ (Dubai International Financial Centre).

⁵⁸ Cf this practical problem in nineteenth-century colonial administration: Indian Contract Act 1872: text at 21.24.

memory sticks, physical weight has become no real problem. Instead, the problem is the 'tsunami' of electronic information.

- 21.20 However, the portents are not favourable. One of the aims of the 1998 English civil procedure code (the Civil Procedure Rules 1998) was to achieve 'simplicity'.⁵⁹ In fact, it has quickly evolved into a lush and complex code.⁶⁰ Excessive detail and repetition have defeated Lord Woolf's admirable aim to concentrate on fundamental principles and leading rules. Furthermore, experience in codified systems has shown that judicial decisions by the more important courts soon become an important appendage to the legislative text. In some instances, notably the French law of tort, the giant edifice of the law rests on the support of a handful of rather vacuous provisions in the code. Experience shows, therefore, that a clean new code does not remain free from judicial glosses for long. Even if England and Wales were to adopt a code for contract law, it would not be long before practitioners were rummaging in the case law to find out 'what the code really means'.
- 21.21 *Dominance of case law in English contract law.* Students of English contract law are expected to learn many leading cases, and indeed casebooks bulging with minor ones. They soon learn the characteristic 'string' effect of cases: that a leading case has a number of smaller decisions, which establish a 'line of cases'. Most English contractual doctrines of contract law are dominated by case law, notably, offer and acceptance, consideration, intent to create legal relations, mistake, misrepresentation, duress, undue influence, unconscionability or exploitation, certainty, breach, frustration, interpretation, remedies and illegality.
- 21.22 *Contexts where statute predominates.* Admittedly, statute, rather than case law, is the dominant source in some areas of English contract law. Examples are: the conferring of rights upon third parties by the Contracts (Rights of Third Parties) Act 1999 (7.34), the control of unfair or unreasonable exclusion clauses by the Unfair Contract Terms Act 1977 (15.08) and the control of unfair clauses in consumer contracts by the Unfair Terms in Consumer Contracts Regulations 1999 (15.33).
- 21.23 *Contexts where statute and common law are intertwined.* There have been several incursions of statute into fields which nevertheless remain dominated by judicial law, notably, the Law Reform (Frustrated Contracts) Act 1943 (16.21), the Law Reform (Contributory Negligence) Act 1945 (18.50) and the Misrepresentation Act 1967 (9.14). These statutes are relatively minor. But they have become problematic. They have not been successfully implanted within the flesh of the common law. These provisions have reminded us that judicial decision-making is flexible, but legislation is fixed, and Parliament's aims are not always obvious. The result is a tension between pliable (judicial) and inflexible (legislative) law.

59 N. Andrews, *English Civil Justice: Progress and Remedies: Nagoya Lectures* (Shinzan Sha Publishers, Tokyo, 2007), chapter 2.

60 See www.dca.gov.uk/civil/procrules_fin/index.htm.

- 21.24 *Attempts at codifying the common law system of contract law.* The Indian Contract Act 1872,⁶¹ a codification of the common law's general principles of contract law, continues to apply in the Indian subcontinent. It has been supplemented by the local courts and by parallel case law development in London (and elsewhere in the common law world). It is interesting that this legislation crossed the Indian Ocean and was adopted in some of the former British colonies in East Africa (for example, in Kenya).
- 21.25 The Scottish and English Law Commissions combined to produce a draft Contract Code (the project ran from 1965 to 1973).⁶² Treitel, the greatest living contract scholar in the UK, was heavily involved.⁶³ The Scots pulled out in 1973.⁶⁴ The project was eventually 'suspended'. The draft (not yet cast into statutory form) was published much later, but in Italy. The foreign place of publication is significant: the modern codification project was sent into exile, like Ovid or Napoleon (but see Dubai's codification of English contract law, 21.28).⁶⁵ Writing nearly thirty years after the collapse of this project, Treitel expressed no regret that it had not come to fruition:⁶⁶

In retrospect, [the decision indefinitely to suspend the project] seems to have been a sound one. Codification of contract law faces a dilemma. In common law countries that have codes of ... contract law (such as India and the Field Code States in the United States) the vague language of the relevant codes has done little, if anything, to improve the 'clarity and accessibility' of contract law which were the Law Commission's declared aims in launching the project. A more precise and detailed Code along the lines envisaged in the Law Commission's Seventh Annual Report in 1972 might have helped to promote these objectives, but only ... at the expense of an unacceptable degree of rigidity.

And he concluded:

On balance ... the decision to 'suspend' the process was indeed a fortunate one; development by judicial activity, and, where appropriate, by legislation reforming specific parts of the subject, has proved to be the preferable option.

- 21.26 Distinct from general contract codes, there are the mini-codes on specific English contracts: the Bills of Exchange Act 1882, the Partnership Act 1890, the Sale of Goods Act 1893 (now 1979) 1979, the Marine Insurance Act 1906 and the Arbitration Act 1996 (the 1882, 1893 and 1906 Acts were drafted by Chalmers: see his entry in the appendix to this

61 On William Macpherson, the main architect, see C. MacMillan, *Mistakes in Contract Law* (Oxford, 2010), 108 ff.

62 Harvey McGregor QC, *Contract Code: Drawn up on Behalf of the English Law Commission* (Milan, 1993); J. Cartwright, 'The English Law of Contract: Time for Review?' (2009) 17 *European Review of Private Law* 155, 168 ff.

63 G. H. Treitel, *Some Landmarks of Twentieth Century Contract Law* (Oxford, 2002), 4–9.

64 *Ibid.*, at 8.

65 This recent codification of the common law rules of contract is available at www.difc.ae/laws-regulations/ (Dubai International Financial Centre).

66 G. H. Treitel, *Some Landmarks of Twentieth Century Contract Law* (Oxford, 2002), 8.

book). For the most part, the legislature has here codified parts of the common law: before their enactment, the law consisted of a mosaic of judicial decisions. Thus, Lord Mustill has commented on how the English law of arbitration, before the 1996 enactment, could only be deduced by reading a mountain of cases. He and Mr Boyd famously scaled that peak.⁶⁷

- 21.27 *Uniform law projects*. There is a great deal of formal written law in the field of transnational carriage of goods.⁶⁸ These are examples of internationally agreed ‘uniform’ law which have been incorporated into English law.
- 21.28 *Sincerest form of flattery*. The Dubai International Financial Centre has produced a codification of English contract law, for use in arbitration or other litigation conducted in Dubai.⁶⁹ This is not ‘English law’, but rather English law as refined, modified and codified by the advisors to the Dubai authorities (the advisors and draftsmen were English experts). However, both in form and in content, this twenty-first-century foreign code might portend the future in England.
- 21.29 *Problems with the case law technique*. Code drafters can start with clean sheets of paper and produce a pleasingly coherent set of provisions, delineating categories, sub-categories, rules and sub-rules, and identifying overarching principles. The author has participated in this process, in Rome, in the field of civil procedure: the American Law Institute/UNIDROIT’s *Principles of Transnational Civil Procedure* (2000 to 2004)⁷⁰ (on which the author has commented in 2009).⁷¹ By contrast, the system of common law decision-making is haphazard. It depends on the adventitious selection by claimants and appellants of disputes and issues to be litigated and taken on appeal. Indeed, this led Lord Radcliffe to observe that the House of Lords (now the Supreme Court) has little real opportunity to keep lower court decisions under review.⁷² Furthermore, common law decisions are also long and difficult to unravel. The process of working out the substance of the rule can occupy people in hours of reading. Discovering the law is a time-consuming, skilled and specialist craft, and the answers are not always rock-solid. Finally, the true rule can remain uncertain – at least at its edges – for many years, even for decades. A good example is the eventual ‘cleansing of the common law’ concerning compensation for late payment of debts (see the *Sempra* case (2007)⁷³ at 18.64); but a counter-example is the baroque mix of common law and equity encrusting the rule in

67 M. Mustill and S. Boyd, *Commercial Arbitration* (London, 2001) (and earlier editions).

68 For English legislation incorporating such international shipping conventions, see *Treitel* (12th edn, London, 2007), 7-090 n. 478.

69 Available at www.difc.ae/laws-regulations/ (Dubai International Financial Centre).

70 Accessible at www.unidroit.org/english/principles/civilprocedure/main.htm. Also published as *ALI/UNIDROIT: Principles of Transnational Civil Procedure* (Cambridge, 2006).

71 N. Andrews, ‘The Modern Procedural Synthesis: The American Law Institute and UNIDROIT’s “Principles and Rules of Transnational Civil Procedure”’ (2008) 164 *Revista de Processo* 109 (Brazil) also published in (2009) *Tijdschrift voor Civiele Rechtspleging* 52 (Netherlands).

72 Lord Radcliffe (1973) 36 MLR 559, reviewing L. Blom-Cooper and G. Drewry, *Final Appeal: A Study of the House of Lords in its Judicial Capacity* (Oxford, 1972).

73 [2007] UKHL 34; [2008] 1 AC 561.

Pinnel's Case (1602),⁷⁴ a rule reluctantly followed by the House of Lords in *Foakes v. Beer* (1884)⁷⁵ (5.45 to 5.63), exposition of which requires careful analysis of an intricate network of rules and exceptions.

21.30 *Distilling the common law.* Against this, it must be noted that the long tradition of English case law has produced a finely meshed set of decisions covering most of the obvious points, many of the less obvious ones, and even some of the really bizarre ones (such as the contractual liability of those who supply defective remedies for influenza,⁷⁶ or who fail to ensure that pig-nut hoppers are properly ventilated, resulting in the death of 254 pigs).⁷⁷ Furthermore, the common law of contract is capable of clear, detailed, even minute statement by textbook writers. Thus, the great contract books by Chitty⁷⁸ and Treitel⁷⁹ (and, as recent generations of students can attest, slimmer 'handbooks', for example McKendrick's)⁸⁰ provide a clear exegesis of extensive case law. These excellent books bridge the communication gap between the law reports and those who clamour for a quick answer. After all, most practitioners have less than a day to find the legal answer (or even an approximate one) to a commercial client's demand for rapid advice. Of course, there are lacunae and loose ends within this body of case law. But most of these are quite trifling. Or, if the gap looks at first quite large, in practice one can often predict quite confidently how, say, an experienced adjudicator, such as a Commercial Court judge, would decide the matter.⁸¹ There is enough litigation before the English High Court and Court of Appeal to keep the common law system revolving and refreshed (although Cartwright has noted the relative paucity of contract cases proceeding to the Supreme Court).⁸²

21.31 *Reluctance to abandon the case law tradition.* Some influential English judges and jurists are hostile to the notion of codifying contract law. This attitude cannot be dismissed as mere complacency, or conservatism, or sentimental attachment to hard law painfully absorbed over decades of study and practice. Instead, the underpinning considerations are as follows. First, the current law works tolerably well, so why try to fix it? England and Wales is a unified jurisdiction. One can contrast the USA, where there are many State jurisdictions within a federal entity. Americans receive

74 (1602) 5 Co Rep 117a (entire Court of Common Pleas).

75 (1884) 9 App Cas 605, HL.

76 *Carlill v. Carbolic Smoke Ball Co.* [1893] 1 QB 256, CA.

77 *Parsons Ltd v. Uttley Ingham & Co.* [1978] QB 791, CA; the common law has been described by Tony Allen, Director of the Centre for Effective Dispute Resolution (CEDR) in London, as 'a coral reef made up of the dead bodies of litigants (and their bankrupted estates)'.

78 *Chitty on Contracts* (30th edn, London, 2008).

79 *Treitel* (12th edn, London, 2007).

80 E. McKendrick, *Contract Law* (8th edn, London, 2009).

81 On the quality of Commercial Court judges, see N. Andrews, *English Civil Justice: Progress and Remedies: Nagoya Lectures* (Shinzan Sha Publishers, Tokyo, 2007), 3-03.

82 J. Cartwright, 'The English Law of Contract: Time for Review?' (2009) 17 *European Review of Private Law* 155, 162 n. 29, noting that, in 2007, only seven House of Lords decisions concerned substantive contract law.

nationwide guidance from the 'Restatement of Contracts' and from the 'Uniform Commercial Code'. Secondly, the pragmatic strength of English contract law derives from its having been laid down and refined in response to real cases. It is not abstract and over-intellectual doctrine, the lucubration of law professors. Instead, the common law consists of propositions 'hammered out on the anvil' of adversarial debate in the courtroom.⁸³ Forensic debate can be intense. In the highest courts, debates between counsel can occupy days, involving meticulous reference to dozens of precedent decisions, both English and foreign. Furthermore, English judges are not snatched from the lecture halls and placed in the highest judicial chamber, as happens in some jurisdictions (although some English judges were briefly academics before entering practice and acting for clients).⁸⁴ All English judges have had experience, often over several decades, as practitioners, mostly as barristers. Thirdly, the courts, especially the appellate courts, have been slow to permit doctrines to emerge or develop in ways which would render English law uncertain⁸⁵ or substantively out of step with the reasonable expectations of business people. Proof of the law's attractiveness is that English contract law is often chosen by 'transnational' contracting parties as the applicable law.⁸⁶ Negotiation of commercial contracts and resolution of disputes arising from them are big international business. London lawyers take a good slice of that business. Finally, it is not unreasonable for English lawyers to be resistant to academically inspired pan-European projects. One might tolerate, even admire, British loyalty to the political and socio-economic programme of the European Union. But this continental commitment is to be weighed against the benefits of preserving the precious and remarkable legacy of the common law. More generally, is it not preferable that competition between legal systems should continue, rather than be stifled by adherence to worldwide or European uniformity?

- 21.32 *Enhancing the law's accessibility within the foreign market.* Perhaps pressure to produce a blending of common law and various civil law traditions might one day prove irresistible. The present signs, however, are that, within England and Wales, there is no imminent wish to abandon the contract rules of the common law in favour of a code. But what if the position were to change? In what way might a contract code be introduced? I would suggest that there are five possibilities:

83 Cf Lord Steyn in *Attorney-General v. Blake* [2001] 1 AC 268, 291, HL: 'Exceptions to the general principle that there is no remedy for disgorgement of profits against a contract breaker are best hammered out on the anvil of concrete cases.' Generally on that decision, see 18.57 ff.

84 Modern judges who have held academic positions for more than four years in British universities include: Lord Goff (Lincoln College, Oxford), Baroness Hale (University of Manchester), Lord Hoffmann (University College, Oxford), Lord Rodger (New College, Oxford), Sir Patrick Elias (Pembroke College, Cambridge) and Sir Jack Beatson (Oxford and Cambridge); with the exception of Beatson, appointment to the High Court occurred after they had already ceased to hold academic positions; some judges have held visiting professorships, notably Lord (Lawrence) Collins.

85 A possible exception is *Attorney-General v. Blake* [2001] 1 AC 268, 291, HL: see 18.57 ff.

86 N. Andrews, *English Civil Justice: Progress and Remedies: Nagoya Lectures* (Shinzan Sha Publishers, Tokyo, 2007), 3-06.

- (1) A global contract code, perhaps influenced by UNIDROIT's *Principles of International Commercial Contracts*.⁸⁷ Such a code might be implemented as mandatory for commercial and consumer contracts within English law; but it is highly unlikely that English lawyers will favour renunciation of the common law inheritance in the name of global harmonisation.
- (2) A European code, perhaps based on either of the non-binding European codes already drafted (see 21.01 for references). Such a code might become mandatory for commercial and consumer contracts or for either of these fields. There are well-organised juristic movements which have been promoting the concept of European harmonisation, especially in the field of private law (see material cited at 21.01). The common law has become besieged.
- (3) An international common law code, representing the synthesis of English, Australian, Canadian, New Zealand, US and other common law jurisdictions (such a code might be mandatory in the relevant jurisdictions). But the USA is legally autonomous; the Commonwealth nations have become independent-minded members of a common law diaspora; final appeal to the Privy Council in London, the umbilical cord, has been severed in nearly all instances (no such appeals take place any longer from Australia, Canada, Hong Kong or New Zealand). In short, the historical ties of common law kinship are much weaker than the competing forces of nationalism and geographical distance.
- (4) A purely English contract code which is mandatory (although perhaps restricted either to consumer or non-consumer matters).
- (5) A purely English contract code, not binding on anyone, but capable of being chosen as the applicable law by parties, notably by those engaged in commerce.

21.33 It would be interesting (not least for the drafting team involved) for England to experiment with the last possibility (see point (5) in the previous paragraph). If such a code proved problematic or unpopular, the experiment could be scrapped. No lasting damage would have been done. The common law would continue to grow organically in the meantime. Conversely, if the experiment were to prove successful, perhaps contract law based on the English common law of contract would eventually be superseded by legislation. English lawyers should keep an open mind to the possibility of: improving substantive law; rendering it still more up to date and predictable; jettisoning some of its doctrinal baggage; re-examining some of its rigidities; refining some of its rules; and taking advantage of other legal systems' good ideas. The author's modest suggestion, therefore, is that the English Commercial Bar, or perhaps the Ministry of Justice, should commission lawyers to produce such a contract code.

⁸⁷ 2nd edn, Rome, 2004; see M. J. Bonell (ed.), *The UNIDROIT Principles in Practice: Case Law and Bibliography on the UNIDROIT Principles of International Commercial Contracts* (2nd edn, Ardsley, NY, 2006); S. Vogenauer and J. Kleinheisterkamp (eds.), *Commentary on the UNIDROIT Principles of International Commercial Contracts* (Oxford, 2009).

21.34 Parties could explicitly adopt the contract code (see (5) at 21.32, and 21.33, for comment) by using appropriately worded ‘choice of law’ clauses (12.05). Whether such a choice-of-law option should be confined to transactions having a ‘transnational’ feature would be open to debate. The author has commented elsewhere on the importance of maintaining resort to the Commercial Court in London.⁸⁸ The contract code could be frequently updated. Commentaries would follow. These would link the contract code with both case law developments and pre-existing case law.⁸⁹ In this way, the foreign litigant would receive the benefit of being able readily ‘to look up a point of English contract law’. This might enhance English law’s position in the global market-place.

88 N. Andrews, *English Civil Justice: Progress and Remedies: Nagoya Lectures* (Shinzan Sha Publishers, Tokyo, 2007), chapter 3; on the question of ‘proof of foreign law in English civil proceedings’, *ibid.*, at chapter 5, and referring to other literature.

89 Lord Diplock, however, considered that the English do not understand that a code requires abandonment of all that precedes: remarks in his Green Lecture, ‘The Law of Contract in the Eighties’ (1981) 15 *University of British Columbia Law Review* 371; however, compare Lord Halsbury LC’s remark, in *Vagliano Bros v. Bank of England* [1891] AC 107, HL, concerning the need to treat codification as a fresh start: ‘I am wholly unable to adopt the view that, where a statute is expressly said to codify the law, you are at liberty to go outside the code so created, because before the existence of that code another law prevailed.’ That said, the temptation to refer backwards in order to explicate relatively stark propositions of law is likely to prove irresistible to both advisors and adjudicators.

Appendix: A who's who of contract law

This list does not include jurists who have not yet retired from their judicial or academic posts.¹

Lord Ackner

Desmond Ackner, 1920–2006. His father was a Jewish dentist from Vienna who settled in London. Desmond Ackner attended Highgate School and Clare College, Cambridge (where he later became an Honorary Fellow). Bencher of the Middle Temple. He began with Economics at Clare, but changed to Law. Called to the Bar in 1945, becoming a QC in 1961, he became a celebrated and successful advocate in the 1960s in several fields (described by Sir Michael Kerr, *As Far as I Remember* (2002), 320–1, as an ‘all-rounder’) (Lord Ackner, even in his eighties, was still an impressive after-dinner speaker). Appointed a High Court judge, 1971; sat in the Commercial Court from 1973; Court of Appeal, 1980; House of Lords, 1986. His judgment on reliance loss in *C & P Haulage v. Middleton* (1983, CA) (18.26) is important (coincidentally, Sir Michael Hutchison, also an *alumnus* of Clare College, refined this doctrine in *CCC Films v. Impact Quadrant Ltd* (1985); burden of proof in this context: 18.26). But Lord Ackner’s most important contribution is *Walford v. Miles* (1992), where he gave the leading speech (‘lock out’ agreements valid, if fixed in time; and invalidity of an agreement to bargain in good faith: 2.07 to 2.10). His daughter, Claudia Ackner, is (as was her father) a judge and a Bencher of the Middle Temple.

Baron Alderson

Edward Hall Alderson, 1787–1857. Charterhouse; private tutor; Gonville and Caius College, Cambridge; Inner Temple. Called to the Bar, 1811. In 1830, without having taken silk, he was appointed judge of the Court of Common Pleas. In 1834, he became a Baron of the Exchequer. His juristic legacy is his judgment in *Hadley v. Baxendale* (1854) (18.42), still the starting point for any exposition of the doctrine of contractual remoteness of damage.

¹ Main sources: *Dictionary of National Biography*; and A. W. B. Simpson, *Biographical Dictionary of the Common Law*, 1984).

American contributors

See the references to the textbook writers, Williston and Farnsworth at 14.16; to Corbin at 7.16; to Lon Fuller at 18.23 and 18.24; and to Justice Benjamin Cardozo at 14.08 and 18.29.

Anson, Sir William

Sir William Anson, 1843–1914. Eton and Balliol College, Oxford; Fellow of All Souls College, Oxford, 1867; Warden of All Souls, 1881. Of his *Principles of the English Law of Contract* (1879), Victor Tunkel writes (in Simpson, *Biographical Dictionary of the Common Law* (1984), 11): '[I]t largely shaped the modern law itself ... He established what has become the familiar order of treatment, discovering the principles underlying the cases and rationalising them under his concepts.' A. G. Guest in the twenty-fifth edition of Anson's textbook (1979) said: '[H]is great quality lay in his ability to expound, with simplicity and felicity, complex principles of law, covering a large field with astonishing completeness.' P. S. Atiyah, *The Rise and Fall of Freedom of Contract* (Oxford, 1979), 682–4, considers Anson's contract textbook, noting that Anson acknowledged that he derived intellectual encouragement from Pollock's publication in 1875, although he derived more information from Leake's rather more 'practitioner-orientated' book of 1867. Lord Diplock noted that contract law was at first the only English subject taught in the new Law School in Oxford in the late nineteenth century, all the other substantive subjects being Roman law: 'The Law of Contract in the Eighties' (1981) 15 *University of British Columbia Law Review* 371. The latest edition is the 29th edition, published in 2010, by Sir Jack Beatson, Andrew Burrows and John Cartwright. On Anson's influence in respect of mistake doctrine, see C. MacMillan, *Mistakes in Contract Law* (Oxford, 2010), 169 ff.

Atiyah, Patrick

Patrick Selim Atiyah, born 1931. Woking County Grammar School; Magdalen College, Oxford; Inner Temple. Called to the Bar, 1956; academic jobs, London School of Economics and Khartoum, 1954–9; civil servant, legal department, Board of Trade, 1961–4; Fellow of New College, Oxford, 1964–9; Chairs in Law, Australian National University, 1970–3; Warwick, 1973–7; Oxford, 1977–88 (retiring, a decade early, because of ill-health). A remarkably prolific writer. His books include: *Vicarious Liability in the Law of Torts* (1967); *Accidents, Compensation and the Law* (1970, now 2006, edited by Peter Cane); *Consideration in Contracts: A Fundamental Restatement* (Canberra, 1971); *The Rise and Fall of Freedom of Contract* (Oxford, 1979); *Promises, Morals, and Law* (Oxford, 1981); *Essays on Contract* (Oxford, 1986); *Pragmatism and Theory in English Law* (1987) (Hamlyn Lecture Series); *Form and Substance in Anglo-American Law* (Oxford, 1987) (with R. S. Summers); *An Introduction to the Law of Contract* (5th edn, Oxford, 1995; 6th edn, 2005, by S. Smith); *Atiyah's Sale of Goods* (12th edn, 2010) (with H. MacQueen and J. Adams); and *The Damages Lottery* (Oxford, 1997). His writing comprises analytical,

contextual, philosophical and historical studies of English contract law, and he pioneered the contextual study of tort law in England in *Accidents, Compensation and the Law* (1970, now 2006, edited by Peter Cane). Work of homage: P. Cane and J. Stapleton (eds.), *Essays for Patrick Atiyah* (Oxford, 1991).

Lord Atkin

James Atkin, born Brisbane, 1867–1944. Christ College, Brecon; Magdalen College, Oxford; Gray's Inn. Called to the Bar in 1891, he practised in the chambers of Thomas Scrutton (and later sat with him as a Lord Justice in the Court of Appeal, for example in *Re Moore* in 1921). Lewis, *Dictionary of National Biography*, says of his advocacy style that it was 'one of gentle but resourceful persuasion, the angler, rather than the tragedian, who could cast flies over the judges'. Appointed, High Court, 1913; Court of Appeal, 1919; House of Lords, 1928. He is the legendary father of the modern 'super tort' of negligence, in *Donoghue v. Stevenson* (1932), and he was the magniloquent dissenter in *Liversidge v. Anderson* (1941), concerning executive power in wartime. In the law of contract, his most famous judgments are: *Balfour v. Balfour* (1919, CA) (intent to create legal relations) (6.08, 6.09) and *Bell v. Lever Bros Ltd* (1932, HL) (mistake) (6.08, 6.09, 10.05 to 10.07, 10.15, 10.17 (see C. MacMillan, *Mistakes in Contract Law* (Oxford, 2010), 272 ff)). But he also participated in *Re Moore & Co. and Landauer & Co.* (1921, CA) and *Arcos v. Ronaasen* (1933, HL) (both cases, promissory conditions, Sale of Goods Act) (both 17.36); *Cellulose Acetate Silk Co. Ltd v. Widnes Foundry Ltd* (1933, HL) (penalty clauses) (19.20); *Shirlaw v. Southern Foundries (1926) Ltd* (1940, HL) (intent to create legal relations: where, however, MacKinnon LJ's judgment in the Court of Appeal has been adopted) (13.09 ff); and the *Fibrosa* case (1943, HL) (total failure of consideration; recovery of payment) (16.21). Biography: Geoffrey Lewis, *Lord Atkin* (Oxford, 1999).

Benjamin, Judah Philip

Judah Philip Benjamin, born St Croix, West Indies, 1811–1884. Practised as an attorney in Louisiana and Washington; active in the politics of the Confederates; first Jewish American Senator. Fled to England 1865. Called to the English Bar, Lincoln's Inn, 1866 (aged 55). 'In 1868 appeared Benjamin's work on the contract of sale (*Benjamin on Sales*), a classic upon this subject in English law. Its success was immediate and complete both in England and America. A second edition appeared in 1873, and a third, the revision of a portion of which was Benjamin's last task before his health gave way, was brought out in 1883' (*Dictionary of National Biography*, J. A. Hamilton, revised H. C. G. Matthew). Current edition: *Benjamin on Sale* (7th edn, London, 2006). On Benjamin's influence in respect of mistake doctrine, see C. MacMillan, *Mistakes in Contract Law* (Oxford, 2010), 123 ff.

Lord Bingham, OM

Thomas Bingham, born London, 1933–2010. Sedbergh School; Balliol College, Oxford; Gray's Inn. Called to the Bar, 1959; QC, 1972; appointed to the High Court, 1980; to the

Court of Appeal, 1986; Master of the Rolls, 1992–6; Lord Chief Justice, 1996–2000; Senior Law Lord, 2000–8. Renowned as a magisterial and pellucid judgment writer and as one of the most distinguished judges of the modern age. He illuminated many branches of the law, including contracts, where his notable judgments include: *Interfoto Picture Library Ltd v. Stiletto Visual Programmes Ltd* (1989, CA) (incorporation of harsh terms) (15.02, 21.04); *Blackpool and Fylde Aero Club v. Blackpool Borough Council* (1990, CA) (common law obligations during tender process) (3.50); *'The Super Servant Two'* (1990) (self-induced frustration) (16.15, 16.19); *Watts v. Morrow* (1991, CA) (mental distress damages in contract) ('very object of a contract' test now modified by *Farley v. Skinner* (2002, HL), both at 18.34); *Philips Electronique Grand Publique SA v. British Sky Broadcasting Ltd* (1995, CA) (implied terms) (13.14 ff); *Banque Bruxelles Lambert* case (1995, CA) (liability of valuer; decision precipitated 'scope of duty' test in the House of Lords) (18.47); *Jaggard v. Sawyer* (1995, CA) (damages in lieu of an injunction) (18.21, 18.23, 18.60); *BCCI v. Ali* (2001, HL) (no separate 'equitable' rules of construction of written contracts) (1.25); *Geest plc v. Lansiquot* (2002, PC) (burden of proof and mitigation doctrine) (18.49); *Director-General of Fair Trading v. First National Bank* (2002, HL) (unfair terms and 1999 Regulations) (15.36, 15.38, 21.07); *HIH Casualty and General Insurance Ltd v. Chase Manhattan* (2003, HL) (exclusion clauses and fraud) (1.09, 15.05); *'The Starsin'* (2004) ('Himalaya' clause; exclusion clauses and third parties) (7.64); and *'The Golden Victory'* (2007, HL) (damages to reflect subsequent events: Lord Bingham dissenting) (18.48). Work of homage: M. Andenas and D. Fairgrieve (eds.), *Tom Bingham and the Transformation of the Law: A Liber Amicorum* (Oxford, 2009)² (notably Sir Bernard Rix, 'Lord Bingham's Contributions to Commercial Law', at 665 ff); Lord Phillips, *ibid.*, xlvii, rated him one of the three best advocates of his generation, the other two being Robert MacCrindle and Robert Alexander; and for a detailed 'biographical sketch', R. Cranston, *ibid.*, li–lxxii. Bingham's extra-judicial writing includes *The Business of Judging* (Oxford, 2000).

Birks, Peter Brian Herrenden

Peter Brian Herrenden Birks, born Sussex, 1941–2004. Chislehurst and Sidcup Grammar School; Trinity College, Oxford; University College, London. Lecturer, University College, London, 1967–71; Fellow, Brasenose College, Oxford, 1971–81; Professor, Edinburgh, 1981–8, Southampton 1988–9, Regius Professor of Civil Law, All Souls College, Oxford, 1989–2004. Peter Birks was one of the author's teachers: Roman Law, Trust, Delict, and Restitution, at Oxford (BA, 1977–80, and BCL, 1981–2). Birks' main works are: *An Introduction to the Law of Restitution* (Oxford, 1984) and *Unjust Enrichment* (2nd edn, Oxford, 2005). But there was a flood of articles, especially after 1983, when his rate of production increased from one or two a year to four or five. He handed over undergraduate contract teaching to Hugh Collins in the mid-1970s at Brasenose (now Professor, London School of Economics, and a major contributor to contract scholarship). Birks' early passion was Roman Law (in which he later held Chairs at Edinburgh and Oxford), but this was

2 Reviewed by C. J. S. Knight, (2010) 126 LQR 148.

overtaken by his zeal for restitution and unjust enrichment. Through his writing, but especially through his teaching, his scholarly example and his boundless academic enthusiasm, his great influence on private law is likely to endure for many years (on his formidable 'intellectual stable', see the list of monographs stimulated and nurtured by his supervision of DPhil students, (2009) 125 LQR 175, 176). *English Private Law* (Oxford, 2000), many contributors, edited by Birks, expresses his ambitious vision of a rational restatement of the whole field (a second edition is edited by Andrew Burrows, a former pupil, and prolific writer on restitution, remedies and contract). Main sources: *Dictionary of National Biography* by W. Swadling. Works of homage: A. Burrows and A. Rodger (eds.), *Mapping the Law: Essays in Memory of Peter Birks* (Oxford, 2006); and C. Rickett and R. Grantham (eds.), *Structure and Justification in Private Law; Essays for Peter Birks* (Oxford, 2008).

Lord Blackburn

Colin Blackburn, born Scotland, 1813–1896. Edinburgh Academy; Eton College; Trinity College, Cambridge; Lincoln's Inn. Called to the Bar, 1838. Gareth Jones, in the *Dictionary of National Biography*, says of Lord Blackburn: 'He was the antithesis of the suave advocate: his humour was dry, his personality grave.' Without having become a QC, he was appointed a judge of the Queen's Bench in 1859, and in 1876 a Lord of Appeal in Ordinary, retiring in 1886. He then lived on his Scottish estate until his death in 1896. 'One of the "creative minds in a creative age"' (C. MacMillan, *Mistakes in Contract Law* (Oxford, 2010), quoting C. H. S. Fifoot, *Judge and Jurist in the Reign of Victoria* (London, 1959), 135). Notable judgments on contract law: *Tweddle v. Atkinson* (1861) (privity) (7.04); *Taylor v. Caldwell* (frustration) (1863) (see C. MacMillan, in C. Mitchell and P. Mitchell (eds.), *Landmark Cases in the Law of Contract* (Oxford, 2008), 167 ff) (16.02, 16.03, 16.08); *Kennedy v. Panama, New Zealand and Australian Royal Mail Co.* (1867) (fundamental error induced by misrepresentation, at common law; cited by Lord Blackburn himself in *Mackay v. Dick* (1881) and cited by the House of Lords in *Bell v. Lever Bros Ltd* (1932) (10.06)); *Smith v. Hughes* (1871) (error at common law) (3.67: see J. Phillips, in C. Mitchell and P. Mitchell (eds.), *Landmark Cases in the Law of Restitution* (Oxford, 2006), 205 ff); *Lindsay v. Cundy* (1876) (10.26) (mistake of identity; cited 'audaciously', in preference to the House of Lords decision in that case, by Denning LJ in *Solle v. Butcher* (1950), 10.26); *Smith v. Chadwick* (1884) (inducement and misrepresentation) (9.04); *Foakes v. Beer* (1884) (accord and satisfaction rule at common law: 5.48: M. Lobban in C. Mitchell and P. Mitchell (eds.), *Landmark Cases in the Law of Restitution* (Oxford, 2006), 223); see also, not cited in this textbook, *Bolton v. Madden* (1873) (consideration); *Erlanger v. New Sombrero Phosphate Co.* (1878) (equitable restitution in integrum) (see also on Blackburn's influence, J. Cartwright, 'The English Law of Contract: Time for Review?' (2009) 17 *European Review of Private Law* 155, 158 n. 14).

Bonell, Michael Joachim

Michael Joachim Bonell, Professor of Comparative Law at the Law Faculty of the University of Rome I 'La Sapienza' (1986 until his recent retirement); Consultant at the

International Institute for the Unification of Private Law (UNIDROIT), Rome (since 1978). Amongst his many publications: *An International Restatement of Contract Law – The UNIDROIT Principles of International Commercial Contracts* (3rd edn, Irvington, NY, 2005); *The UNIDROIT Principles in Practice: International Caselaw and Bibliography on the UNIDROIT Principles of International Commercial Contracts* (2nd edn, Ardsley, NY, 2006); and *Un ‘Codice’ internazionale del diritto dei contratti* (2nd edn, Milan, 2006). He is the inspired and diligent architect of the UNIDROIT project, from its inception to its second edition (see 21.01 ff on UNIDROIT’s *Principles of International Commercial Contracts*).

Lord Browne-Wilkinson

Nicolas Browne-Wilkinson, born 1930. Lancing; Magdalen College, Oxford; Lincoln’s Inn. Called to the Bar, 1953; QC, 1972; appointed to the High Court, 1977; to the Court of Appeal, 1983; Vice-Chancellor, Chancery Division, 1885–91; House of Lords, 1991–2000. His practice in Chancery, combined with a shrewd sense that technical doctrine and procedures are not ends in themselves, made him a penetrating and pragmatic judge (he was critical of the baroque process and decision in *Tito v. Waddell (No. 2)* (1977) (18.29), the Pacific islanders’ case, in which he had been counsel). His leading judgments on contract law are: *Swiss Bank Corporation v. Lloyds Bank Ltd* (1979) (third party interference with contracts) (7.73); *Multiservice Bookbinding Ltd v. Marden* (1979) (unconscionability) (11.37); *Johnstone v. Bloomsbury Health Authority* (1992, CA) (implied terms) (13.07, 13.20); *Smith New Court Securities Ltd v. Scrimgeour Vickers (Asset Management) Ltd* (1997, HL) (deceit) (9.12); *Barclays Bank plc v. O’Brien* and *CIBC v. Pitt* (1994, both HL) (11.23, 11.24, 11.30 ff); the *Panatown* case (2001, HL) (privity: promisee’s damages) (7.27); and the *Workers Trust* case (1993, PC) (common law relief against forfeiture of deposits) (19.35).

Chalmers, Sir Mackenzie Dalzell

Sir Mackenzie Dalzell Chalmers, born Nonington, Kent, 1847–1927. King’s College, London; Trinity College, Oxford; Inner Temple. Called to the Bar, 1869; county court judge (1884–96); civil servant (1896–1908), India, First Parliamentary Counsel (1902), Home Office, London (Permanent Secretary, 1903); later representative at the Hague (1910–12). He drafted codifying Bills which led to the Bills of Exchange Act 1882, the Sale of Goods Act 1893 (now 1979) and the Marine Insurance Act 1906; author of twelve books, mostly on specific contracts.

Cheshire, Geoffrey Chevalier

Geoffrey Chevalier Cheshire, born Cheshire, 1886–1978. Denstone; Merton College, Oxford; Lincoln’s Inn. Fellow, Exeter College, Oxford, 1912–44; Vinerian Professor of English Law, All Souls College, Oxford, 1944–9. His *Law of Contract* (1945), co-written with C. H. S. Fifoot, became a favourite among students and judges. Cheshire wrote three

major textbooks, on land law, private international law, and contract, which have survived in successive editions. F. H. Lawson (formerly Fellow of Merton College, Oxford; Professor of Comparative Law, Brasenose College, Oxford) in the *Dictionary of National Biography*, said: 'It seems highly unlikely that Cheshire's feat of writing such major works on three completely different subjects will ever be repeated.' On Cheshire's approach to mistake doctrine, see C. MacMillan, *Mistakes in Contract Law* (Oxford, 2010), 287 ff. Cheshire's son, Leonard, was a distinguished RAF officer, awarded the Victoria Cross.

Chitty, Joseph

Joseph Chitty, born London, 1796–1838. Westminster School; Middle Temple. A member of the Chitty dynasty (Simpson, *Biographical Dictionary of the Common Law* (1984), 111–13) and five 'lawyer' Chittys (*Dictionary of National Biography*). His *A Practical Treatise on the Law of Contracts Not Under Seal* (1826) is now *Chitty on Contracts* in its thirtieth edition. Simpson, *Biographical Dictionary of the Common Law* (1984), 112, comments on Chitty that it has been 'edited so as to have little real connection with the original except the mystery of legal apostolic succession'.

Clarke, Malcolm

Malcolm Alistair Clarke, born 1943. Kingswood School, Bath, St John's College, Cambridge. Fellow of St John's College, Cambridge since 1970, and Professor of Commercial Contract Law, University of Cambridge, 1999–2010. Renowned in particular for his erudition in both the law of transport (numerous works, including *Contracts of Carriage by Land and Air* (2nd edn, Richmond, 2008)) and the law of insurance (*The Law of Insurance Contracts* (5th edn, London, 2006); and *Policies and Perceptions of Insurance in the Twenty-First Century* (Clarendon Law Series, Oxford, 2005)). He has also taught general contract law since 1970, and contributed to general work in that field, notably, his 'Vitiating Factors' (misrepresentation, mistake, duress, etc.) in *Butterworths Law of Contract* (3rd edn, London, 2007), 775–986.

Lord Denning

Alfred Thompson ('Tom') Denning, born Hampshire, 1899–1999. Andover Grammar School; Magdalen College, Oxford (first in mathematical moderations in 1917; first in mathematics, 1920); Royal Engineers, 1917–19. Taught mathematics at Winchester for a year. Attended a one-year law course at Magdalen College, Oxford, and achieved a first in jurisprudence. Lincoln's Inn. Called to the Bar, 1923; KC, 1938; judge of the High Court, 1944; Court of Appeal, 1948; House of Lords, 1957. In 1962, he was appointed Master of the Rolls, in the Court of Appeal, retiring in 1982. Main sources: Lord Denning, *The Family Story* (1981); Lord Denning, *The Closing Chapter* (1983); Iris Freeman, *Lord Denning: A Life* (1993); E. Heward, *Lord Denning: A Biography* (2nd edn, London, 1997); J. Jowell and J. McAuslan, *Lord Denning: The Judge and the Law* (London, 1984); J. Getzler, in P. Cane and J. Conaghan (eds.), *New Oxford Companion to Law* (Oxford,

2008), 306. His judicial career was so long and his influence so extensive that he came close to monopolising judicial development of the common law in this jurisdiction: J. Jowell and J. McAuslan, *Lord Denning: The Judge and the Law* (London, 1984). It suffices to say that his judgments appear throughout this text. Some decisions or ideas have been discarded, notably, his attempt to control exclusion clauses by declaring them ineffective in the face of fundamental breach, repudiated, not for the first time, in *Photo Production Ltd v. Securicor Transport Ltd* (1980, HL) (15.06); his remarks on ‘inequality of bargaining power’ in *Lloyds Bank v. Bundy* (1975) (11.42, 11.43); and the *Solle v. Butcher* (1950, CA) (10.13 to 10.15) doctrine of shared mistake in equity. Other decisions have put down roots: notably the Court of Appeal’s endorsement in *Collier v. Wright (Holdings) Ltd* (2007, CA) (15.59, 15.60) of the *High Trees* (1947) (5.56 ff) line of cases concerning the extinction of a debt following the creditor’s promise to receive part-payment and to release the unpaid part. As for Denning’s regard for precedent, Lord Phillips has said: ‘He had a wide knowledge of the common law that he sometimes used eclectically to support the result that he considered accorded with the ends of justice’ (M. Andenas and D. Fairgrieve (eds.), *Tom Bingham and the Transformation of the Law: A Liber Amicorum* (Oxford, 2009), xlviii). More generally, Robert Goff, in the *Dictionary of National Biography*, said: ‘Denning reminded a whole generation of lawyers that the duty of a judge is not merely to apply the law but to do justice; and that, if justice was to be done according to law, the common law could not stand still – it must be developed to respond to the needs of justice in a living society ... He was one of the greatest and most influential judges ever to sit on the English bench. Some would maintain that the title of this country’s greatest judge of all time should still be awarded to Lord Mansfield ... the father of commercial law. Nevertheless, few would dispute that Denning was the greatest English judge of the twentieth century.’

Lord Devlin

Lord Devlin, born Kent, 1905–1992. Stonyhurst; Christ’s College, Cambridge; Gray’s Inn. Called to the Bar, 1929, KC, 1945. Appointed to the High Court, 1948; Court of Appeal, 1960; House of Lords, 1961, resigned 1964 (at the age of 58, having found the work uncongenial). He had been a very successful commercial barrister. His judicial career also contained many highlights. However, in contract law, there is surprisingly little that remains centrally important: contrast his more important contribution to tort law, notably, *Hedley Byrne & Co. v. Heller* (1964) (negligent misstatement) (5.17); and *Rookes v. Barnard* (1964, HL) (exemplary damages). His discussion of anticipatory breach is perhaps his most significant contribution to contract law: *Universal Cargo Carriers Corporation v. Citati* (1957) (17.09, 17.14); see also *Parker v. Clark* (1960) (intent to create legal relations) (6.11); *Heaven & Kesterton Ltd v. Etablissements Francois Albiac et Cie* (1956) (mitigation) (18.49); and *Ingram v. Little* (1961, CA, dissenting) (error as to identity) (10.33). His wide-ranging intellectual gifts were formidable. His works included: *Trial by Jury* (1956) (Hamlyn Lectures); *Samples of Lawmaking* (1962); *The Enforcement of Morals* (1965) (part of the famous ‘Hart/Devlin’ debate on the connection between law and positive

morality); *Too Proud to Fight: Woodrow Wilson's Neutrality* (1974); *The Judge* (Oxford, 1979); *Easing the Passing: The Trial of Dr John Bodkin Adams* (1985); and *Taken at the Flood* (1996) (autobiography). Tony Honoré comments, in P. Cane and J. Conaghan (eds.), *New Oxford Companion to Law* (2008), 312: 'Of the small number of twentieth-century English judges who addressed a wider public, his rigorous conscience, clarity, and eloquence made him the most impressive writer.' Lord Scarman said: 'Patrick Devlin was one of the truly great intellects of the twentieth century. He excelled in legal practice as a barrister: he excelled as a judge – at all levels: and he was an inspirational jurist' (preface to Devlin's *Taken at the Flood* (1996)). This was not a bad recovery from a Cambridge '2:2' in Law (*ibid.*, 72). He also participated in the Law Commission's project on the codification of contract law (21.25).

Lord Diplock

Kenneth Diplock, born Croydon, 1907–1985. Whitgift School; University College, Oxford (Chemistry); Middle Temple. Called to the Bar, 1932; KC, 1948; appointed to the High Court, 1956; Court of Appeal, 1968; House of Lords, 1968. A major influence on the development of contract law in the second half of the twentieth century (B. Dickson, 'The Contribution of Lord Diplock to the General Law of Contract' (1989) 9 OJLS 441). His influence derives partly from his steadfast adherence to traditional principle, overturning in the House of Lords aberrant decisions of Lord Denning's Court of Appeal (notable examples are *Gibson v. Manchester City Council* (1979) (3.05) and *Photo Production Ltd v. Securicor Ltd* (1980) (15.06)). Diplock was famously associated with the rise of the 'intermediate' or 'innominate' term, in *Hongkong Fir Shipping Co. Ltd v. Kawasaki Kisen Kaisha Ltd* (1962) (17.31). Diplock was an analytical lawyer of the highest calibre: for example, *Harvela v. Royal Trust Company of Canada* (1986) (3.54); and see his Cecil and Ida Green lecture, 'The Law of Contract in the Eighties' (1981) 15 *University of British Columbia Law Review* 371. However, he was prone to terminological vanity, preferring not to call a spade a spade, but a bilateral contract a 'synallagmatic' agreement: 'Every synallagmatic contract contains in it the seeds of the problem: in what event will a party be relieved of his undertaking to do that which he has agreed to do but has not yet done?' (*Hongkong Fir* case (1962)): repeated in *United Dominions Trust (Commercial) v. Eagle Aircraft Services* (1968): 'In [the *Hongkong Fir*] case, I was careful to restrict my own observations to synallagmatic contracts. The insertion of this qualifying adjective was widely thought to be a typical example of gratuitous philological exhibitionism.' He had read chemistry at Oxford, and there is a suggestion that his approach to law was driven by the need to categorise. His addresses to students in Middle Temple Hall, where he was a Bencher, were legendary: austere and suggesting 'zero tolerance' of human fallibility. However, he smoked (cigarettes) a lot. Towards the end, suffering from short-windedness (emphysema), he 'would take gulps from an oxygen cylinder in his room, before going into court in the House of Lords to deliver a brilliantly analytical speech' (private source). In the *Dictionary of National Biography*, S. Cretney and G. Le Quesne comment on Diplock's

'fun side': 'Moments of bonhomie tended to be characterised ... by what a colleague later described as a "smile that would have done credit to any shark". Diplock was a passionate ... fox-hunter. The guest list for the Middle Temple's "Grand Day" in 1974, the year of his Treasurership, included the Duke of Beaufort and seven masters of hounds.' He also participated in the Law Commission's project on the codification of contract law (21.25).

Farnsworth, (Edward) Allan³

Born Providence, Rhode Island, 1928–2005. University of Michigan (maths); Yale (physics); Columbia (law). Taught at Columbia, 1954 until his death. He 'was considered the foremost legal authority on contracts in the United States' (American Law Institute's newsletter). His major treatise is *Farnsworth on Contracts* (3rd edn, updated posthumously 2008) in three volumes. A one-volume 'hornbook' is *Contracts* (4th edn, 2004). ALI Director, Lance Liebman (also Columbia), said of Farnsworth's contribution as Reporter for the *Restatement of the Law Second, Contracts* (1981): '[T]he widely used three-volume set remains a triumph of the ALI. This project, which Farnsworth worked on for over ten years, required a professor who knew everything about contract law and was very balanced, progressive, and forward-looking.' Farnsworth also sat on the Working Group on UNIDROIT's *Principles of International Commercial Contract*: see also Bonell and Furmston.

Furmston, Michael

Michael Furmston, born 1933. Wellington School; Exeter College, Oxford; University of Birmingham; Gray's Inn. Called to the Bar 1960. Lecturer, University of Birmingham, 1957–62; Queen's University, Belfast, 1962–3; Fellow, Lincoln College, Oxford, 1964–78; Professor, University of Bristol, 1978–98; Dean, School of Law, Singapore Management University, 2007; counsel in the *Ruxley* case (18.29); English contributor to the UNIDROIT *Principles* (21.01 ff). He has become a 'spine' name on *Cheshire, Fifoot, and Furmston's The Law of Contract* (from 8th edn, 1972, to 15th edn, 2007). And he is the editor of another leading work: *Butterworths Law of Contract* (3rd edn, London, 2007). There are many other books on aspects, or types, of contract (for example, M. Furmston and G. J. Tolhurst, *Contract Formation: Law and Practice* (Oxford, 2010)).

Lord Goff

Robert Goff, born 1926. Eton; New College, Oxford; Inner Temple. Called to the Bar, 1951; Fellow of Lincoln College, Oxford, 1951–5; in practice at the commercial bar, 1955–75; appointed to the High Court, 1975, to the Court of Appeal, 1982, to the House of Lords, 1986, Senior Law Lord, 1996–8. Having entered practice, he co-wrote, with Gareth Jones,

3 I am grateful to the American Law Institute's newsletter for these details.

the leading work on the *Law of Restitution* (1966) (now 7th edn, London, 2007), although the lion's share of later editions was borne by his academic co-author. After he became a judge, he disclaimed any ability as an advocate, suggesting that his talent in the courtroom had been confined to flattering his opponent, the witnesses and the judge. His acute and measured intelligence pervades his judgments which were consistently outstanding. Highlights include: the *British Steel* case (1984) (failure of contract; restitutionary award) (2.04, 18.55); *BP v. Hunt (No. 2)* (1979) (exposition of Law Reform (Frustrated Contracts) Act 1943) (16.22 ff); *Amalgamated Investments Ltd v. Texas Bank* (1981) (estoppel by representation) (5.62, 5.69); '*The Pegase*' (1981) (remoteness of damage) (18.44); *Allied Marine Transport Ltd v. Vale do Rio Doce Navegacao SA ('The Leonidas D')* (1985) (formation of contracts; inactivity and silence) (3.12); '*The Evia Luck*' (1992) (duress) (11.05); '*The Mahkutai*' (1996) ('*Himalaya*' clause; jurisdiction clause) (7.65 ff); and the *Panatown* case (privity; promisee's damages) (7.30). Work of homage: W. Swadling and G. Jones (eds.), *The Search for Principles: Essays in Honour of Lord Goff of Chieveley* (Oxford, 1999), containing (appendix) his British Academy, Maccabaeian Lecture, 'The Search for Principle' (1983).

Goode, Sir Roy

Royston Miles Goode, born 1933. Highgate School; University of London, External LLB; Inner Temple. Solicitor, 1955, partner Mishcons, 1966–71. Called to the Bar, 1988; QC, 1990; Chair in Law, Queen Mary College, London, 1971–90; Norton Rose Professor of English Law, University of Oxford, 1990–8; Fellow, St John's College, Oxford, 1990 onwards. The *doyen* of English commercial lawyers, with a huge international reputation. His main works are: *Hire-Purchase Law and Practice* (2nd edn, 1970; supplement 1975); *The Hire Purchase Act 1964* (1964); *Hire-Purchase and Conditional Sale: A Comparative Survey of Commonwealth and American Law* (1965) (with J. S. Ziegel); *Introduction to the Consumer Credit Act, 1974*; *Consumer Credit Law and Practice* (looseleaf); *Consumer Credit* (1978); *Commercial Law in the Next Millennium* (London, 1998) (Hamlyn Lecture Series, 1997); *Commercial Law* (3rd edn, London, 2004); *Legal Problems of Credit and Security* (3rd edn, London, 2003); *Payment Obligations in Commercial and Financial Transactions* (1983); *Proprietary Rights and Insolvency in Sales Transactions* (2nd edn, London, 1989); *Principles of Corporate Insolvency Law* (3rd edn, 2005); and Roy Goode, Herbert Kronke, Ewan McKendrick and Jeffrey Wool, *Transnational Commercial Law: International Instruments and Commentary* (Oxford, 2007). Work of homage: R. Cranston (ed.), *Making Commercial Law: Essays in Honour of Roy Goode* (Oxford, 1997).

Guest, Anthony

Anthony Gordon Guest, born Devon, 1930. Colston's School, Bristol; St John's College, Oxford; Gray's Inn. Called to the Bar, 1956; Benchers 1978. After teaching at Oxford (Fellow of University College, Oxford, 1955–65), he became Professor of Law, King's College, London, 1966–97, maintaining a prolific contribution to both general contract law and specific commercial contracts, notably: *Anson's Principles of the Law of*

Contract (21st to 26th edns, 1959–84); *Chitty on Contracts* (Assistant Editor, 22nd edn, 1961; General Editor, 23rd to 27th edns, 1968–94; Assistant Editor, 28th to 30th edns, 1999–2008); *The Law of Hire-Purchase* (1966); General Editor, *Benjamin's Sale of Goods* (1974–2006); a joint editor of the *Encyclopedia of Consumer Credit* (1975); a joint editor of *Introduction to the Law of Credit and Security* (1978); and editor of *Chalmers and Guest on Bills of Exchange* (14th to 17th edns, 1991–2009).

Lord Hobhouse

John Stewart Hobhouse, born Liverpool (Hobhouse's father was a wealthy ship-owner), 1932–2004. Eton; Christ Church, Oxford; Inner Temple. Called to the Bar, 1955; QC, 1973. Hobhouse practised in commercial law, initially shipping. '[H]is great rival at the commercial bar' was Mustill (*per* Lord Lloyd, obituary for Hobhouse, *The Guardian*). Hobhouse could be direct as an advocate, as Lord Mance, in the *Dictionary of National Biography*, demonstrates: 'After a famously choleric member of the Court of Appeal declined to listen further to an argument, Hobhouse replied that this showed a lack of intellectual curiosity, and on another occasion he invited the same member of the court to turn his mind elsewhere, so that Hobhouse might address his two colleagues.' Hobhouse was appointed to the High Court, 1982, to the Court of Appeal, 1993, and to the House of Lords, 1998, where he sat until illness forced him to retire, in 2004. His penetrating legal mind is apparent in his first instance decision in the 'swaps' litigation: *Westdeutsche Landesbank Girozentrale v. Islington London Borough Council* (1994): 'In the case of *ultra vires* transactions such as those with which I am concerned where there ... never has been any contract, I prefer to use the phrase "absence of consideration"'.⁴ Accepted in later case law, this concept, secreted in the cases meticulously analysed by Hobhouse, ultimately led Birks to sense that his own theory might unravel and hence to renounce some of the analysis in *An Introduction to the Law of Restitution* (Oxford, 1984), substituting *Unjust Enrichment* (2nd edn, Oxford, 2005) (Birks and Hobhouse had memorably held an oral debate, in the presence of Gareth Jones, on this question at the Restitution group meeting at the University of East Anglia in the mid-1990s). As for Hobhouse's contribution to 'mainstream' contract law, highlights are: *Forsikringsaktieselskapet Vesta v. Butcher* (contributory negligence; now bedrock, unless there is legislative change) (18.49); *County Ltd v. Girozentrale Securities* (1996) (mitigation) (11.48); and the *Etridge* case (2002) (undue influence) (11.24 ff). Hobhouse notably dissented in the *Blake* case (2001, HL) (account of profits for breach of contract) (18.55 ff, 18.59). He also gave a pungent speech (10.30 ff) as a member of the majority in *Shogun Finance Ltd v. Hudson* (2004) (10.29 ff; 14.31) (compare the lengthy dissents by Lords Millett and Nicholls). At [55] in that case, he thundered: '[T]he ... fundamental principles of law to be applied ... are not in dispute ... [T]he further learned, but ultimately unproductive, discussion of them will warm academic hearts. But what matters is the principles of law. They are clear and sound and need no revision. To cast doubt upon them can only be a disservice to English

4 [1994] 4 All ER 890, 924.

law.' Hobhouse was an enemy of codification, and he abhorred lack of rigour (which he perceived in some 'soft law' projects or international conventions) (21.01). He kept bees and climbed mountains, latterly hills.

Lord Hoffmann

Leonard Hoffmann, born South Africa, 1934. South African College School; University of Cape Town; Queen's College, Oxford; Gray's Inn. Called to the Bar, 1964. He had partly overlapping careers (Oxford to London train) as an academic and as a barrister. He was an Oxford law don (University College, Oxford, 1961–73), becoming Reader in Evidence. And he was a barrister, specialising in Chancery work, QC, 1977 (earlier in South Africa, 1958–60). He was appointed to the High Court, 1985, to the Court of Appeal, 1992, and to the House of Lords, 1995, from which he retired in 2009, having for several decades been widely respected as an unusually brilliant legal mind. His contribution to the art and mystery of interpretation of written contracts (notably the *Investors Compensation* case, 14.07) has secured him a major intellectual influence upon the law's development. He was not slow, however, to spot the need for commercial certainty and 'bright line' doctrine: for example, the *Union Eagle* case (1997, PC) (17.40) concerning the equitable doctrine of forfeiture of proprietary interests; and his admirably restrictive speech in *Co-operative Insurance Services v. Argyll Stores Ltd* (1998) (18.19) has become the leading discussion of specific performance in modern commercial practice.

Hopkins, Cherry

Life Fellow of Girton College, Cambridge; legendary teacher of obligations (contract, tort and commercial law); regular contributor to the *Cambridge Law Journal*. Her former pupils at Girton include the two most senior female English judges to have made contributions to the law of contract: Baroness Hale, a Lord of Appeal in Ordinary (17.38, 18.42 case (5), 18.45), and Dame Mary Arden, a Lady Justice of Appeal (5.46, 5.48, 5.60, 9.02, 11.37, 14.12, 14.37, 15.34).

Sir George Jessel

Born Savile Row, London, 1824–1883. Neumegen's School for Jews, Kew; University College, London; Lincoln's Inn. Called to the Bar, 1847, practised as a conveyancer and in the Rolls Court (then a court of first instance); QC, 1865; Solicitor-General, 1871, at Gladstone's request; Master of the Rolls, 1873 (then a court of first instance; in 1881, the Master of the Rolls ceased to be a judicial office of first instance, and so in 1881–3 he sat as Master of the Rolls in the Court of Appeal). He was the first Jew to hold high judicial office in England (A. L. Goodhart, *Five Jewish Lawyers of the Common Law* (1949)). Jessel's father was Zadok Aaron Jessel, a diamond merchant. Jessel was very learned in equity, and seldom reserved judgment. On these two aspects, Gareth Jones, in the *Dictionary of National Biography*, comments: '[H]e considered himself third in the pecking order of great English equity judges, after two Lord Chancellors,

the towering Lord Hardwicke and Lord Cairns ... A remarkable memory combined with mastery of the subject matter enabled him never to reserve a judgment in the Rolls courts and only very occasionally in the Court of Appeal, and then only at the instigation of his brethren.' Jessel's judgment in *Redgrave v. Hurd* (1881, CA) is the seminal discussion of (1) the capacity to rescind for a wholly innocent misrepresentation (9.02) and (2) absence of a duty to check the accuracy of a material misrepresentation (9.04 at proposition (5)).

Jones, Gareth

Gareth Hywel Jones, born 1930, Wales. Porth County School; St Catherine's College, Cambridge; University College London; Harvard; Lincoln's Inn. Called to the Bar, 1955; academic posts, Oriel and Exeter Colleges, 1956–8; King's College London, 1958–61; Trinity College, Cambridge, 1961 onwards; Downing Professor of the Laws of England, 1975–98; former Chairman of the Law Faculty, Cambridge. His *magnum opus*, of which he long ago became the main editor because of his co-author's professional demands, is R. Goff and G. H. Jones, *The Law of Restitution* (1st edn, London, 1966; 7th edn, London, 2007). His other works are: *The History of the Law of Charity 1532–1827* (1969); *The Sovereignty of Law* (1973); *Restitution in Public and Private Law* (Bombay, 1991); and Jones and Goodhart, *Specific Performance* (2nd edn, London, 1996). Amongst private lawyers of the last fifty years, his versatility places him in a very special category, having written or taught at the highest level in the fields of contract, legal history, remedies, restitution or unjust enrichment, trusts and equity. Moreover, he was in demand as a teacher of trusts and equity in the USA. Work of homage: W. Cornish, R. Nolan, J. O'Sullivan and G. Virgo (eds.), *Restitution: Past, Present and Future: Essays in Honour of Gareth Jones* (Oxford, 1998).

Kerr, Sir Michael

Michael Kerr, born Berlin, 1921–2002. Aldenham School; Clare College, Cambridge; later Honorary Fellow; Lincoln's Inn. S. Cretney, in the *Dictionary of National Biography*, says of Kerr's upbringing in Germany: 'Both his parents were of Jewish descent ... Their household was cultured ... Albert Einstein, Gerhart Hauptmann, Arthur Schnitzler, H. G. Wells, and Bernard Shaw were family friends.' Called to the Bar by Lincoln's Inn, 1948; QC, 1961; appointed to the High Court, 1972; Chairman of the Law Commission, 1979–81; appointed to the Court of Appeal, 1981–9. He was an expert on arbitration and an outstanding commercial lawyer, as an advocate, on the bench, and as an arbitrator. Sir Lawrence Collins described him as a 'very experienced and eminent commercial judge'.⁵ In '*The Siboen and The Sibotre*' (11.16, 11.21), Kerr was the first English judge to recognise 'economic duress' as a vitiating factor. Other interesting contributions are: '*The Karen Olmann*' (1976) (interpretation of written contracts), although that decision has now been rejected (14.17 to 14.20); '*The Odenfeld*' (1978) (innocent party and repudiatory

5 [2008] EWCA Civ 183; [2008] 2 All ER (Comm) 387, at [122].

breach) (18.10); *B & S Contracts & Design Ltd v. Victor Green Publications Ltd* (1984, CA) (economic duress) (11.20); *Thake v. Maurice* (1986, CA) (dissenting) (medical assurance: intent to create legal relations) (3.71); and *Dean v. Ainley* (1987, CA) (damages for repair of premises) (18.31). In his autobiography, *As Far As I Remember* (Oxford, 2002), he describes internment as an 'alien' during the early part of the Second World War (he was arrested in Cambridge with the late Professor Kurt Lipstein, later Fellow of Clare). Of Robert Goff's elevation to become a Lord of Appeal in Ordinary, instead of himself, Kerr magnanimously wrote: 'I recognised at the time how much more an academic and more scholarly lawyer could contribute to the House of Lords than a purely pragmatic one like me' (*As Far As I Remember* (Oxford, 2002), 321).

Leake, Stephen Martin

Stephen Martin Leake, born London, 1826–65. King's College School, Cambridge; St John's College, Cambridge; Middle Temple. Called to the Bar, 1853. Practised for ten years. Became interested in legal science, and (as Sir John Baker, *Dictionary of National Biography*, explains) 'worried by increasing deafness, he made the decision to leave practice and retire to his father's seat in Hertfordshire. There he became a county magistrate and made use of the comparative leisure of country life to compose lucid and methodical treatises on the law.' Baker continues: 'His *Principles of the Law of Contracts* (1867) was the first scientific treatise on what was soon to become a core subject in the legal curriculum; it was also the first treatise to identify and analyse some recently developed doctrines, such as vitiation by mistake. The book was to exercise a beneficial effect on the academic legal literature of the next generation; it was the basis of an American textbook by W. A. Keener, published in 1891, and its influence in English universities was acknowledged by Sir William Anson.' Leake also co-wrote with Bullen (Leake's former pupil master) *Precedents of Pleadings in Common Law* (1860) (now the 16th edition of *Bullen & Leake & Jacob's Precedents of Pleadings* (2007)). Leake also wrote an *Elementary Digest of the Law of Contracts* (1878). Leake's fifth son, Arthur Martin-Leake, (1874–1953), was twice awarded the Victoria Cross (1902, South Africa; 1914, Ypres). On Leake's influence in respect of mistake doctrine, see C. MacMillan, *Mistakes in Contract Law* (Oxford, 2010), 112 ff.

MacKinnon, Sir Frank

Frank MacKinnon, born London, 1871–1946. Highgate; Trinity College, Oxford; Inner Temple. Called to the Bar in 1897; QC, 1914; appointed to the High Court, 1924; and to the Court of Appeal, 1937, where he sat until, in 1946, 'walking to work at the law courts ... he suffered a heart attack and died soon afterwards' (Rubin, *Dictionary of National Biography*). He is famous for having formulated the 'officious bystander' test in *Shirlaw v. Southern Foundries (1926) Ltd* (1939, CA) (13.10 ff) (although this test was earlier stated by Scrutton LJ (MacKinnon's former pupil-master) in *Reigate v. Union Manufacturing Co. (Ramsbottom) Ltd* (1918, CA) (13.10)). He also assisted in the editing of *Scrutton on Charterparties and Bills of Lading*.

McGregor, Harvey

Harvey McGregor, born 1926. Inverurie Academy; Scarborough Boys' High School; Queen's College, Oxford; Harvard; Inner Temple. Called to the Bar, 1955; QC, 1978; Fellow of New College, Oxford, 1972–85, and Warden, 1985–96. He has edited *McGregor on Damages* (as it is now known) since the twelfth edition (1961) (the current edition is the eighteenth (2009); previously, it was a book by Mayne). He was also active in the Law Commission's project to codify the English law of contract in the 1960s, which was eventually published by him as *English Draft Contract Code* (Milan, 1993). His work on damages is a lucid and comprehensive treatment of a dense and fast-moving topic: a *tour de force*.

Lord Mansfield

William Murray, born Scotland, 1705–1793. Perth Grammar School; Westminster; Christ Church, Oxford; Lincoln's Inn. Called to the English Bar, 1730; becoming an MP, Solicitor-General and Attorney-General. In 1756, he was appointed Chief Justice of the Court of King's Bench, and was created 'Lord Mansfield'. Two of Lord Mansfield's stimulating decisions on contract law were overruled: in *Pillans v. Van Mierop* (1765),⁶ his idea that simple writing would be a substitute for consideration was reversed by the House of Lords in *Rann v. Hughes* (1778) (5.10); and, in *Hawkes v. Saunders* (1782), he suggested that moral obligation could ground liability for the promise made in recognition of past services, but this was rejected by Lord Denman in *Eastwood v. Kenyon* (1840) (5.21). But Lord Mansfield's enduring contribution is to insurance law, notably the seminal decision in *Carter v. Boehm* (1766)⁷ concerning pre-contractual disclosure in insurance law (9.34). He became the 'benchmark' of great English judges: see the comparisons drawn between Lord Mansfield and (1) Lord Atkin by Viscount Simon LC in the Chamber of the House of Lords, 27 June 1944;⁸ (2) Sir Thomas Scrutton by Llewellyn;⁹ and (3) Lord Denning, by Lord Goff.¹⁰ Generally, see C. H. S. Fifoot, *Lord Mansfield* (Oxford, 1936); J. Oldham, *English Common Law in the Age of Mansfield* (Chapel Hill, NC, 2004); John Adams, in Simpson, *Biographical Dictionary of the Common Law* (1984), 378–84; and the literature cited in the *Dictionary of National Biography* (J. Oldham); cf Brian Simpson, (1975) 91 LQR 247, who finds it ironic that Mansfield should be regarded as the quint-essentially creative judge: '[T]he innovative judge ... has become part of the folklore of the profession, incongruously typified by the arch conservative Lord Mansfield.' See also,

6 (1765) 3 Burr 1663; G. McMeel, in C. Mitchell and P. Mitchell (eds.), *Landmark Cases in the Law of Contract* (Oxford, 2008), 23 ff; S. Waddams, 'Principle in Contract Law: The Doctrine of Consideration', in J. W. Neyers, R. Brough and S. G. A. Pitel (eds.), *Exploring Contract Law* (Oxford, 2009), 51, at 55 ff.

7 S. Watterson, in C. Mitchell and P. Mitchell (eds.), *Landmark Cases in the Law of Contract* (Oxford, 2008), 59 ff.

8 See G. Lewis, *Lord Atkin* (Oxford, 1999), 166.

9 Karl Llewellyn was rich in his praises of Scrutton in an article about him in the *Columbia Law Review* (1936).

10 In *Dictionary of National Biography*.

on Mansfield, J. Cartwright, 'The English Law of Contract: Time for Review?' (2009) 17 *European Review of Private Law* 155, 159.

Lord Millett

Peter Millett, born 1932. Harrow; Trinity Hall, Cambridge; Middle Temple and Lincoln's Inn. Called to the Bar, 1955; QC, 1973; appointed to the High Court, Chancery Division, 1986; to the Court of Appeal, 1994; to the House of Lords, 1998, retiring in 2004. His learning in the field of trusts and equity is prodigious. His main judgments in contract law are: *Alec Lobb (Garages) Ltd v. Total Oil GB Ltd* (1983) (unconscionability doctrine in equity) (11.36); *Gibbon v. Mitchell* (1990) (error and voluntary instruments) (10.22); *Little v. Courage* (1995, CA) (negotiation and best endeavours clauses) (2.08); *Allied Maples Group v. Simmons & Simmons* (1995, CA) (loss of chance damages) (18.32) (dissenting on the facts only); *Jaggard v. Sawyer* (1995, CA) (damages in lieu of injunction) (18.21, 18.23, 18.60); *Jervis v. Harris* (1996, CA) (debt and damages distinction) (18.05); *Freeman v. Niroomand* (1996, CA) (damages for defective building work) (18.29); the *Panatown* case (2001, HL) (damages in third party context) (7.27 ff) (dissenting, 7.30, 7.31, with Lord Goff); *National Commercial Bank (Jamaica) Ltd v. Hew* (2003, PC) (undue influence) (11.28); *Shogun Finance Ltd v. Hudson* (2004, HL) (error as to identity) (10.29 ff) (dissenting, 10.31, with Lord Nicholls; see also 10.37); and his article, 'Equity's Place in the Law of Commerce' (1998) 114 LQR 214.

Lord Mustill

Michael Mustill, born 1941. Oundle School; St John's College, Cambridge (Honorary Fellow, 1992); Gray's Inn. Called to the Bar, 1955; practised in commercial law; QC, 1968; appointed to the High Court, 1978; to the Court of Appeal, 1975; to the House of Lords, 1992, retiring from appeals in 1997. Goodhart Professor of Legal Science, University of Cambridge, 2003–4. With Stewart Boyd QC, author of the leading work on commercial arbitration, *The Law and Practice of Commercial Arbitration in England* (1982; 2nd edn, London, 1989; companion volume, 2001) (21.26); M. Mustill, *Anticipatory Breach: Butterworths Lectures 1989–90* (London, 1990) (17.43); also contributed to *Scrutton on Charterparties and Bills of Lading* and to *Arnould on Marine Insurance*. Friend and chambers colleague of Sir Michael Kerr (for example, in June 1967, Michael Kerr and Michael Mustill appeared in the leading case, *Koufos v. C Czarnikow Ltd ('The Heron II')* (1967) as counsel for the (unsuccessful) appellant owners). Mustill was influential (with Lord Saville, as he now is) in the preparation of the Arbitration Act 1996 (England and Wales). Notable judgments on contract law include: *Regent OHG Aisestadt v. Francesco of Jermyn Street Ltd* (1981) (breach) (17.34); *Atlantic Lines & Navigation Co. Inc. v. Hallam ('The Lucy')* (1983) (section 2(2) of the Misrepresentation Act 1967) (10.27); *Resolute Maritime Inc. v. Nippon Kaiji Kyokai ('The Skopas')* (1983) (section 2(1) of the Misrepresentation Act 1967) (9.16); *Hussey v. Eels* (1990, CA) (mitigation) (18.48); *Malcolm v. Chancellor, etc. of the University of Oxford* (1994, CA) (certainty, intent to create legal relations) (dissenting) (4.12 ff); *Lombard North Central plc v. Butterworth* (1987, CA) (terms) (17.28);

Pan Atlantic Insurance Co. Ltd v. Pine Top Insurance Co. Ltd (1995, HL) (non-disclosure and insurance) (9.09, 9.34 at (5)); *Ruxley Electronics Ltd v. Forsyth* (1996, HL) ('cost of cure' damages; 'consumer surplus' damages) (18.29); *Charter Reinsurance Co. Ltd v. Fagan* (1997, HL) (interpretation of written contracts) (14.01, 14.09, 17.22, 17.26); and *Smith New Court Securities Ltd v. Scrimgeour Vickers (Asset Management) Ltd* (1997, HL) (deceit) (9.12). Since judicial retirement, he has enjoyed a career as a commercial arbitrator.

Lord Nicholls

Donald Nicholls. Birkenhead School; Liverpool University; Trinity Hall, Cambridge; Middle Temple. Called to the Bar, 1958; QC, 1974; appointed to the High Court, Chancery Division, 1983; Court of Appeal, 1986; Vice-Chancellor, Chancery Division 1991–4; House of Lords, 1994, becoming Senior Law Lord, and retiring in 2007. An acute and innovative judge. Notable decisions are: *Gran Gelato v. Richliff* (1992) (misrepresentation) (9.14, 9.15, 9.17); *Jobson v. Johnson* (1989) (penalty clauses) (19.16); *Royal Bank of Scotland v. Etridge* (2002) (undue influence) (11.23 ff); and *Attorney-General v. Blake* (profit-stripping remedy for breach of contract) (18.56 ff). His plea for abolition of the rule barring evidence of negotiations as an aid to interpretation of written contracts (Nicholls, 'My Kingdom for a Horse: The Meaning of Words' (2005) 121 LQR 577) (14.01) did not persuade Lord Hoffmann in *Chartbrook Ltd v. Persimmon Homes Ltd* (2009) (14.15).¹¹

Pollock, Sir Frederick

Frederick Pollock, born London, 1845–1937. Eton; Trinity College, Cambridge (later Fellow, 1868); Lincoln's Inn. Called to the Bar, 1871, but did not practise successfully. He was, like Chitty, a member of a legal dynasty: five other Pollock lawyers are listed in the *Dictionary of National Biography* and in Simpson, *Biographical Dictionary of the Common Law* (1984), 420–4. Gareth Jones, *Biographical Dictionary of the Common Law* (1984), 422, comments: 'Pollock's first book was the *Principles of Contract at Law and in Equity* (1876), followed ... by *The Law of Torts* (1882) ... [His] books were models of lucidity, arrangement and presentation which proved a revelation to the practitioner and an inspiration to the jurist. These qualities are the hall-mark of all his writings, which were prolific and influential.' Richard Cosgrove, in the *Dictionary of National Biography*, says: '[T]hese two books became instant classics ... and continued to exercise influence through posthumous editions.' P. S. Atiyah, *The Rise and Fall of Freedom of Contract* (Oxford, 1979), 682–4, considers Pollock's contract textbook. Pollock also edited the *Law Quarterly Review* from its inception in 1885 until 1919, and was editor-in-chief of the *Law Reports* from 1905 to 1935. Pollock was Professor of Jurisprudence, Oxford, 1883–1903. Lord Dunedin in *Dunlop v. Selfridge* (1915, HL) (5.10) adopted Pollock's definition of consideration. Intellectual biography: Neil Duxbury, *Sir Frederick Pollock and the English*

¹¹ [2009] UKHL 38; [2009] 1 AC 1101, at [41].

Juristic Tradition (Oxford, 2004). On Pollock's influence in respect of mistake doctrine, see C. MacMillan, *Mistakes in Contract Law* (Oxford, 2010), 143 ff.

Lord Radcliffe

Cyril Radcliffe, born Wales, 1899–1977. Haileybury College; New College, Oxford; Fellow of All Souls, Oxford, 1922–37; Inner Temple. Called to the Bar, 1924; KC, 1935; regarded (*per* Robert Armstrong, *Dictionary of National Biography*) as the 'outstanding figure at the Chancery Bar' in the pre-war years. In 1949, he was appointed a Lord of Appeal in Ordinary ('the first man, other than former law officers, for over sixty years to be appointed to the House of Lords direct from the bar'). He retired as a judge in 1964. He became the first Chancellor of the University of Warwick in 1966. For contract lawyers, he is renowned for his trenchant and elegant speech in *Davis Contractors Ltd v. Fareham Urban District Council* (1956, HL), a cornerstone of the doctrine of frustration (16.02, 16.09) (see also N. Duxbury, 'Lord Radcliffe Out of Time' [2010] CLJ 41, for abundant biographical references).

Lord Reid

James Scott Cumberland Reid, born Drem, East Lothian, 1890–1975. Edinburgh Academy; Jesus College, Cambridge; Honorary Benchers, Gray's Inn. Called to the Scottish Bar, 1914; fought in the First World War; KC, 1932; Solicitor-General for Scotland, 1936–41; MP for Hillhead, Glasgow, 1937–48; Lord Advocate, 1941–5; Dean of Faculty of Advocates, 1945–8; appointed a Lord of Appeal in Ordinary, 1948, serving until January 1975 (from 1962, he was the senior law lord, presiding, in the absence of a Lord Chancellor). During his long career in the House of Lords, he made a huge contribution. He had a special talent for trenchant, balanced and precise legal analysis. His most notable contributions to contract law are: *White & Carter v. McGregor* (1962) (debt; anticipatory breach) (18.05 ff); *McCutcheon v. David MacBrayne Ltd* (1964) (objective principle) (1.10, 3.57); '*The Heron II*' (1967) (remoteness of damage) (18.39 ff); *Whitworth Street Estates (Manchester) Ltd v. James Miller & Partners Ltd* (1970) (bar on reference to subsequent conduct; interpretation of written contracts) (14.06); *Schuler (L) AG v. Wickman Machine Tool Sales Ltd* (1974) (condition, innominate term, interpretation) (17.20 ff); *Esso v. Harper's Garage* (1968) (solus agreements, restraint of trade, and public policy) (20.20); and *A Schroeder Music Publishing Co. Ltd v. Macaulay* (1974) (solus agreements, restraint of trade, and public policy) (20.20).

Reynolds, Francis

Francis Reynolds, born 1932. Winchester; Worcester College, Oxford; Inner Temple. Called to the Bar, 1961. Fellow of Worcester College, Oxford, 1960–2000, now emeritus; Professor of Law, University of Oxford, 1992–2000. Editor of the *Lloyd's Maritime and Commercial Law Quarterly* from 1983 to 1987 and of the *Law Quarterly Review* from 1987 onwards. Substantial contributor to practitioner textbooks, notably, *Chitty on Contracts*,

Bowstead and Reynolds on Agency, Benjamin's Sale of Goods, Carver on Bills of Trading and English Private Law. Also ran a course in Oxford on international trade law.

Scrutton, Sir Thomas

Thomas Scrutton, born Poplar, London: 1856–1934. His father was a wealthy ship-owner (like the father of Hobhouse), and Thomas became the nation's expert on shipping law. Mill Hill School; University of London; Trinity College, Cambridge; Middle Temple. Called to the Bar, 1882; part-time Professor of Legal History and Constitutional Law, University College London; KC, 1901. His main works were: *The Contract of Affreightment as Expressed in Charter Parties and Bills of Lading* (1886) (still published as *Scrutton on Charterparties and Bills of Lading*) and *The Laws of Copyright* (1883). Appointed to the King's Bench, 1910, and to the Court of Appeal, 1916. The entry by F. D. MacKinnon (revised by Hugh Mooney) in the *Dictionary of National Biography* describes his chambers while he was a barrister: '[H]e occupied a room in the hideous block called Temple Gardens, and in which a Spartan rigour reigned ... The other two rooms were filled with "devils" and pupils, including, at various times, the future Lord Atkin, Lord Wright [and] Lord Justice MacKinnon.' Especially as a trial judge, Scrutton was often 'brusque, irritable, petulant and rude' (S. Uglow, in Simpson, *Biographical Dictionary of the Common Law* (1984), 468), adding (*ibid.*, 469): '[H]e never "made" the House of Lords, though two of his pupils, Atkin and Wright were appointed while Scrutton was still in the Court of Appeal. Maybe this was a bitter blow to him, but he had made many enemies.' Scrutton often sat with Atkin and Bankes in a famously 'strong' Court of Appeal (in *Dictionary of National Biography*, on Atkin, Lewis writes: 'Scrutton and Atkin constantly disagreed. The arbiter was Bankes who presided with the air of a country gentleman. As Lord Denning put it, "they fought for the body of Bankes"'). The *Dictionary of National Biography* also notes that: 'Karl Llewellyn¹² was rich in his praises of Scrutton in an article about him in the *Columbia Law Review* (1936), declaring him ... "a greater commercial judge than Mansfield"'. In fact, Scrutton's legacy has diminished: few of his judgments are still cited for general principles of contract. Remnants are: *Lens v. Devonshire Club* (1914) (intent to create legal relations) (6.11); *Reigate v. Union Manufacturing etc.* (1918, CA) (implied terms; officious bystander test) (13.10, 13.11); *Re Moore & Co. and Landauer & Co.* (1921, CA) (conditions; termination justified for trivial breach) (17.36); and *Foley v. Classique Coaches* (1934, CA) (certainty) (4.20).

Sealy, Leonard

Leonard Sedgwick Sealy, born Hamilton, New Zealand, 1930. Stratford High School; Auckland University; Gonville and Caius College, Cambridge; in practice as a solicitor and barrister, New Zealand, 1953–5 and 1958–9; teaching member of the Faculty of Law, Cambridge, 1959–1991 (S. J. Berwin Professor of Corporate Law, 1991–7); lectured extensively on contract law (although main research subjects are company law, insolvency law

12 Karl Llewellyn, Columbia University, New York, 'Legal Realist' and commercial law expert.

and commercial law); (with R. Hooley) *Cases and Materials in Commercial Law* (London, 1994; 4th edn, 2008); co-editor of *Benjamin's Sale of Goods* (1974); and general editor of *Benjamin* (7th edn, 2006). Former editor of the *Cambridge Law Journal*; former Chairman of the Law Faculty, Cambridge, and former Senior Tutor of Gonville and Caius College, Cambridge. Also participated in the Law Commission's project on the codification of contract law in the 1960s (21.25).

Lord Steyn

Johan Steyn, born South Africa, 1932. Stellenbosch University; University College, Oxford. Called to the Bar in South Africa, 1958, appointed Senior Counsel in 1970, but left South Africa to settle as a commercial barrister in London, becoming QC in 1979; appointed to the High Court, 1985; Court of Appeal, 1992; House of Lords, 1995. His major judgments in the field of contract law are: *Associated Japanese Bank Ltd v. Crédit du Nord SA* (1989) (mistake) (10.06); *Trentham (Percy) Ltd v. Archital Luxfer* (1993) (offer and acceptance) (3.06); *CTN Cash & Carry Ltd v. Gallaher* (1994) (duress) (11.09); *Vitol SA v. Norelf Ltd* ('The Santa Clara') (1996) (repudiation) (3.12, 17.48); *Smith New Court Securities Ltd v. Scrimgeour Vickers (Asset Management) Ltd* (1997) (deceit and misrepresentation) (9.13, 9.15); *Mannai Investment Co. v. Eagle Star Life Assurance* (1997) (interpretation of written contracts and instruments) (14.06); *Republic of India v. India Steamship Co. Ltd* ('The Indian Endurance') (No. 2) (1998) (estoppel by convention) (5.69); *Equitable Life Assurance Co. Ltd v. Hyman* (2002) (implied terms) (13.12); and *Director General of Fair Trading v. First National Bank plc* (2002) (unfair terms) (15.36, 21.07). His article, 'Contract Law: Fulfilling the Reasonable Expectations of Honest Men' (1997) 113 LQR 433 (4.05, 21.14) and his decision in *First Energy (UK) Ltd v. Hungarian International Bank Ltd* (1993) (21.14) are a call for English law to embrace 'good faith' under the banner of 'reasonable expectations of businessmen'. Lord Steyn had a massive respect for Treitel. In retirement, Lord Steyn has committed himself to civil liberties.

Treitel, Sir Guenter (Heinz)

Guenter Heinz Treitel, born in Germany, 1928. Kilburn Grammar School; Magdalen College, Oxford; Gray's Inn. After teaching at the London School of Economics (1951–3) and at University College, Oxford (1953–4), he became a law don at Magdalen, 1954–79; Vinerian Professor of English Law, All Souls College, Oxford, 1979–96. Sole author of his *The Law of Contract* (eleven editions, 1962 to 2003) (the most recent edition, the twelfth, is by Edwin Peel). Other leading works include: *Remedies for Breach of Contract: A Comparative Account* (Oxford, 1988); *Frustration and Force Majeure* (2nd edn, London, 2004); *Some Landmarks of Twentieth Century Contract Law* (Oxford, 2002); and contributions to *Benjamin's Sale of Goods*, *Chitty on Contracts*, *Carver on Bills of Lading*. Also a contributor to *English Private Law* (Oxford, 2000; 2nd edn, 2007). Work of homage: F. D. Rose (ed.), *Consensus ad Idem: Essays in the Law of Contract in Honour of Guenter Treitel* (London, 1996). His learning in this field is immense. Lynx-eyed, he spotted every material detail. He became the leading authority on English contract law, venerated by

scholars, judges and lawyers. Also participated in the Law Commission's project on the codification of contract law in the 1960s (21.25).

Turpin, Colin Conyngham

Colin Conyngham Turpin, born 1928. LLB, Cape Town; LLB, Cambridge, 1953. Advocate in South Africa. Emeritus Reader in Public Law; Fellow of Clare College, 1961 to present. Former Editor of the *Cambridge Law Journal*. Leading authority and author on constitutional law, principally, *British Government and the Constitution: Text and Materials* (6th edn, Cambridge, 2007, with Adam Tomkins). Besides contributing articles and notes on contract law, Colin Turpin in *Government Contracts* (London, 1972) and *Government Procurement and Contracts* (London, 1989) investigated a complex subject, hitherto known only to Whitehall *cognoscenti*: some light had been earlier shed on this by J. D. B. Mitchell, *The Contracts of Public Authorities: A Comparative Study* (London, 1943). Turpin taught contract law at Cambridge in the Faculty of Law and for the colleges from the early 1960s until the mid-1990s. A group of legal alumni founded the Turpin-Lipstein Fellowship in Law jointly in his honour and in memory of Professor Kurt Lipstein, QC, LL.D (1909–2006; also a Fellow of Clare College, and to whose memory this book is dedicated); and law reading rooms are dedicated separately to Colin Turpin and Kurt Lipstein within Clare College.

Lord Wedderburn of Charlton

Kenneth William Wedderburn, born Deptford, 1927. Aske's Hatcham School; Whitgift School; Queens' College, Cambridge. Called to the Bar, Middle Temple, 1953; QC, 1990; Bencher of Middle Temple, 2008. After teaching at Clare College, Cambridge, 1952–64 (also Honorary Fellow since 1997), he was Cassel Professor of Commercial Law, 1964–92, at the London School of Economics. His main scholarly contributions have been within labour law, company law, and torts. His Cambridge pupils (who include Cherry Hopkins and Leonard Sealy) comment on his brilliance in all branches of private law, including contract law, and his article¹³ on collateral contracts remains seminal. He edited *Sutton and Shannon on Contracts* (7th edn, 1970, with Anthony Grabiner; 6th edn, 1963; and 5th edn, 1956). He was also formerly the editor of the *Modern Law Review*. Work of homage: P. Davies, A. Lyon-Caen, S. Sciarra and S. Simitis, *European Community Labour Law: Principles and Perspectives: Liber Amicorum Lord Wedderburn of Charlton* (Oxford, 1997).

Lord Wilberforce

Richard Orme Wilberforce, born India, 1907–2003. Winchester; New College, Oxford; Middle Temple; Fellow of All Souls College, Oxford, 1932 to death. A descendant of William Wilberforce, the slavery abolitionist. Called to the Bar, 1931; practised at the Chancery Bar until 1939, and from 1947 in other areas; QC, 1954; soldier, 1939–46;

13 [1959] CLJ 58.

civil servant, 1946–7; appointed to the High Court, Chancery Division, 1961; he did not become a Lord Justice of Appeal in the Court of Appeal, and was promoted straight to the House of Lords, 1964. Until his retirement in 1982, he sat in 465 appeals in the House of Lords. Lord Neill, in the *Dictionary of National Biography*, says: '[A]s a judge at the highest level he left a corpus of judgments, covering a huge area of the law, which stand comparison for their scope and brilliance with the judgments of any other British judge of the twentieth century.' He contributed to many leading decisions on the law of contract. Highlights are: the *Suisse Atlantique* case (1966) (breach) (17.07); *Prenn v. Simmonds* (1971) (evidential bar on references to pre-contractual negotiations; interpretation of written contracts) (14.14); *Schuler (L) AG v. Wickman Machine Tool Sales Ltd* (1974) (condition and innominate terms) (dissenting, 'a solitary hawk') (17.20, 17.23, 17.32); *New Zealand Shipping Co. Ltd v AM Satterthwaite & Co. Ltd ('The Eurymedon')* (1975) ('Himalaya' clauses, and observations on offer and acceptance) (3.06); the *Reardon Smith Line* case (1976) (interpretation) (14.06); *Liverpool City Council v. Irwin* (1977) (implied terms) (13.04); *Johnson v. Agnew* (1980) (breach and termination of contracts) (9.22, 17.49) (a magisterial speech); *Photo Production Ltd v. Securicor Transport Ltd* (1980) (exclusion clauses) (15.06) (another stellar speech); *Woodar Investment Development Ltd v. Wimpey Construction UK Ltd* (1980, HL) (breach, and promisee's damages in third party context) (7.23, 17.17); *National Carriers Ltd v. Panalpina (Northern) Ltd* (1981) (leases and frustration) (16.14); *Bunge v. Tradax* (1981) (conditions and termination) (17.19); and *Port Jackson Stevedoring Pty v. Salmond & Spraggon (Australia) Pty ('The New York Star')* (1981) ('Himalaya' clauses) (7.63, 17.48). Work of homage: M. Bos and I. Brownlie (eds.), *Liber Amicorum for Lord Wilberforce* (Oxford, 1987); posthumous autobiography, *Reflections on My Life: Richard Orme Wilberforce* (edited and published by S. Wilberforce (his son), Croydon, 2003). H. L. A. Hart, the legal philosopher, regarded Wilberforce as having the best legal mind of any English lawyer known to Hart (they had been students on the same staircase at New College, reading classics).

Winfield, Sir Percy

Percy Henry Winfield, born Stoke Ferry, Norfolk, 1878–1953. King's Lynn Grammar School; St John's College, Cambridge. Called to the Bar, Inner Temple, 1903. Wounded in action in the First World War. Rouse Ball Chair in Law, Cambridge, 1928. Best known for his huge contribution to the law of torts (notably, *The Law of Tort* (London, 1937); this became the leading textbook, edited since his death primarily by T. Ellis Lewis, J. A. Jolowicz and W. V. H. Rogers; now *Winfield and Jolowicz on Tort* (18th edn, by W. V. H. Rogers, London, 2010)). However, Winfield also contributed to the textbook tradition in contract law: *Salmond and Winfield on Contracts* (1927) (of which the *Dictionary of National Biography* says: '[P]unctiliously enclosing his own contributions within square brackets, he preserved and completed Sir John Salmond's unfinished work'); and three editions of *Pollock on Contracts* (1942–50; finally, 13th edn, London, 1950). See S. J. Bailey, *Sir Percy Henry Winfield* (Oxford, 1955) (from the *Proceedings of the British Academy*, vol. 41).

Lord Wright

Robert Alderson Wright, born South Shields, County Durham, 1869–1964. Early education obscure; Trinity College, Cambridge; Inner Temple. Called to the Bar, 1900, aged 31; lecturer at the London School of Economics; entered Scrutton’s chambers; KC, 1917; appointed to the King’s Bench Division, 1925; promoted straight to the House of Lords, 1932, retiring in 1947; Master of the Rolls, sitting in the Court of Appeal, 1935–7. Remarkable decisions on contracts include: *Vandepitte v. Preferred Accident Insurance Corporation of New York* (1933, PC) (trusts of promises) (7.15); *Liesbosch v. Owners of the Steamship Edison* (*‘The Edison’*) (1933, HL) (the ‘impecuniosity’ doctrine in damages) (18.23); *Maritime National Fish Ltd v. Ocean Trawlers Ltd* (1935, PC) (self-induced frustration) (16.06, 16.18); *With v. O’Flanagan* (1936, CA) (pre-formation falsification of representation) (9.03); *Luxor (Eastbourne) Ltd v. Cooper* (1940, HL) (estate agency; unilateral contract analysis; and implied terms) (3.45, 13.01, 13.08, 13.11); *Joseph Constantine SS Co. v. Imperial Smelting Corporation Ltd* (1942, HL) (self-induced frustration) (16.15). See also the Law Revision Committee, chaired by Lord Wright MR, *Sixth Interim Report on ‘The Statute of Frauds and the Doctrine of Consideration’* (1937, Cmd 5449) (5.48); earlier, Wright, ‘Ought the Doctrine of Consideration to Be Abolished from the Common Law?’ (1936) 49 *Harvard Law Review* 1225.

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Chapter 19 Consensual remedies for breach of contract: liquidated damages and deposits

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Index

- Ackner, Lord
Regent Hotels (UK) Ltd v. Pageguide Ltd (1985), 539
'The Simona' (1989), 485, 508
Walford v. Miles (1992), 19–20, 26
- Aikens J
Harper v. Interchange Group Ltd, 400
Statoil ASA v. Louis Dreyfus Energy Services LP ('The Harriette N') (2008), 82, 86, 292
Trident Turboprop (Dublin) Ltd v. First Flight Couriers (2008), 16, 269
- Alderson, Baron, 525, 560
Hadley v. Baxendale (1854), 659
- American Law Institute, 665, 668
- Andrews, Neil, 211, 212
- arbitration agreements, 636
- arbitration clauses, 99, 215–16, 264, 349, 351
- Arden LJ, 147, 410–11
Collier v. P & MJ Wright (Holdings) Ltd (2007), 156, 158
Devenish Nutrition Ltd v. Sanofi-Anetis SA (2008), 590, 595
Egan v. Static Control Components (Europe) Ltd, 393
Grand Metropolitan plc v. William Hill Group (1997), 394–5, 420, 411
Square Mile Partnership Ltd v. Fitzmaurice McCall Ltd (2006), 393
- Asquith LJ
Combe v. Combe (1951), 129
Victoria Laundry (1949), 560
- assignment, 225–32
 assignment of patents and copyright, 228
 distinction from other doctrines, 231–2
 effects of, 226
 equitable assignment, 225, 228
 extent of the assigned right, 228–30
 damages, 229–30
 modes of, 227–8
 and negotiable instruments, 231
 no assignment of duties, 226–7
 and vicarious performance, 226
 non-assignable rights, 225, 230–1
 and novation, 231
 and revocable mandate, 232
 statutory assignment, 225, 227
 and third party beneficiary rights, 231
- Atkin, Lord, 175
Arcos v. Ronaasen (1933), 503
Balfour v. Balfour (1919), 175–6
Bell v. Lever Bros Ltd (1932), 84, 85, 271, 280–1, 282, 284, 290
Cellulose Acetate Silk Co. Ltd v. Widnes Foundry (1925) Ltd (1933), 609, 610
- Bailhache J, *Wall v. Rederiaktiebolaget Luggud* (1915), 610
- Ball, S., 22
- bargains
 and consideration, 125, 183
 inequality of bargaining power, 308, 340–1, 606
 judicial desire to uphold, 90
 substantive unfairness, 339–40
- Barry J, *William Lacey (Hounslow) Ltd v. Davis* (1957), 347
- Beatson, J., 456
- Benjamin, 503
- Berg, A., 28–30, 392–3, 663
- Bigwood, R., 243, 318, 322
- Bingham LJ, 14, 166, 372, 421–2
Blackpool and Fylde Aero Club v. Blackpool BC (1990), 73
Customs & Excise Commissioners v. Barclays Bank plc (2006), 128–9
Director General of Fair Trading v. First National Bank plc (2002), 439, 440–1, 662
Interfoto v. Stiletto (1989), 660–1
Philips Electronique Grand Publique SA v. British Sky Broadcasting Ltd (1995), 372
'The Super Servant Two' (1990), 463, 465
Walford v. Miles (1992), 25

- Birks, P. B. H., 312, 324, 589
 Blackburn, Lord, 245
 Foakes v. Beer (1884), 147
 Smith v. Hughes (1871), 84
 Taylor v. Caldwell (1863), 377, 448, 449
 Blair J, *Styrdon v. Vendside Ltd* (2009), 363
 Blake principle, 520–1
 Blanesburgh, Lord, *Bell v. Lever Bros Ltd* (1932),
 283, 284–5
 Bowen LJ
 Carlill v. Carbolic Smoke Ball Co. (1893), 67, 68
 ‘*The Moorcock*’ (1889), 361–4
 Re Casey’s Patents (1892), 132–3
 Smith v. Land and House Property Co. (1884),
 239
 Bowsher J, *Pegler Ltd v. Wang (UK) Ltd* (2000), 436
 Bramwell J
 Boulton v. Jones (1857), 304
 Household Fire Insurance Co. v. Grant (1879), 56
 Branson J, *Warner Bros Pictures Inc. v. Nelson*
 (1957), 533
 breach of contract, 8, 127, 253, 475–515
 anticipatory breach, 485–8
 attempted, 519
 impossibility of culpable self-inducement,
 486–8
 rights of the innocent party, 488
 by stating unwillingness to perform, 485–6
 breach of condition or breach of warranty, 502
 conditions (promissory obligations), 476
 ‘condition’ not always used in a technical
 sense, 493–4
 courts’ construal of, 476
 downgrading of conditions, 494–5
 general construction of the contract, 492–3
 importance of timing, 499
 intermediate or innominate terms, 499–501
 interpretation to avoid an unreasonable result,
 495–6
 judicial decisions on, 491–2
 parties agree that a term is a condition, 492
 repetitive breach in continuing contracts, 505
 statutory control in commercial sales, 502–4
 termination clauses, 497
 terms construed as conditions, 492
 when a term is a condition, 491–3
 consensual remedies for, 599–617
 deposits, 612–17
 penalty doctrine, 601–11
 relief against forfeiture of money instalments,
 612
 definition, 475
 the entire obligation rule, 513–15
 express right to terminate, 479–82
 forms of, 476
 anticipatory breach, 476, 477
 bad performance, 478
 breach by non-feasance or misfeasance, 476
 breach of promise not to act, 479
 deliberate breach, 484
 dilatory performance, 476, 478
 explicit anticipatory breach, 478
 inaction or ‘no-show’ on the day of
 performance, 478
 inferred anticipatory breach, 478
 renunciation, 479
 renunciation on the day of performance, 476,
 477
 repudiation of performance, 478
 repudiatory breach, 479, 480, 524
 rights of the innocent party, 479–82
 implied rights to cancel, 479–82
 judicial remedies for. *see* judicial remedies for
 breach of contract, 519–97
 jurisdiction of, 506
 liquidated damages and deposits, 599–617
 mistake and, 279
 penalty doctrine, 599, 601–11
 process of termination for breach, 507–10
 decision effected by conduct or silence, 509–10
 equivocal exercise of the right to terminate,
 509
 new opportunity to terminate, 509
 rights of the innocent party, 507
 and rescission for misrepresentation, 263–5
 relief against forfeiture of proprietary or
 possessory interests, 505–7
 remedies available, 8, 519–97, 599–617
 remoteness and ‘scope of duty’ tests, 566–8
 renunciation on the day of performance, 488–90
 invocation of a wrong reason, 488
 mistaken but good faith statement that non-
 performance is justified, 488–90
 right to cancel without breach, 479–82
 and the right to refuse performance, 477, 482
 rights of the innocent party, 476, 479–82
 binding nature of election, 508
 need to pause for thought, 509
 no third choice, 508
 nominal or substantial damages, 484
 restricted entitlement to terminate, 484–5
 right to elect, 477, 507, 524
 strict or non-strict obligations, 482–4
 termination for, 477, 485, 490–505, 510–13

- breach of contract (*cont.*)
 - termination of contracts of indefinite duration
 - classification of promissory terms, 491–2
 - construction of the contract, 492–3
 - rights of the innocent party, 492
 - a term is construed as a condition, 492
 - when a term is a condition, 491–3
- Bridge, Michael, 526
- Bridge, Lord
 - Butler Machine Tool Co. Ltd v. Ex-Cell-O Corporation (England) Ltd* (1979), 60
 - Chartbrook Ltd v. Persimmon Homes Ltd* (2009), 396, 414, 415
 - Howard Marine and Dredging Co. Ltd v. A. Ogden & Sons (Excavations) Ltd* (1978), 258
 - Scally v. Southern Health Board* (1992), 360–1, 375
- Bridlington Agreement, 366
- Briggs J, 395
 - Chartbrook Ltd v. Persimmon Homes Ltd* (2009), 402
- Brightman J
 - Hart v. O'Connor*, 339
 - Overbrooke Estates v. Glencombe Properties Ltd*, 266
 - Wrotham Park* case, 592
- Brown, Sir Stephen P, *Taylor v. Bhail* (1996), 642
- Brown LJ, Simon, *Economides v. Commercial Union Assurance Co. plc* (1998), 240
- Browne-Wilkinson, Lord
 - CIBC Mortgages plc v. Pitt* (1994), 322, 325
 - Coral Leisure Group Ltd v. Barnett* (1981), 631
 - Johnstone v. Bloomsbury Health Authority* (1992), 375
 - Multiservice Bookbinding Ltd v. Marden* (1979), 334
 - Nash v. Halifax Building Society* (1979), 628
 - Panatown* case (2001), 201, 202
 - Smith New Court* case, (1997), 254–5, 257–8
 - Swiss Bank Corporation v. Lloyd's Bank Ltd* (1979), 222
- Brownsword, R., 664
- Buckley LJ
 - ASLEF* case (1972), 359
 - Bankers Insurance Co. Ltd v. South* (2003), 441
 - Thomas Bates Ltd v. Wyndham's (Lingerie) Ltd* (1981), 414
- Buckmaster, Lord, *May & Butcher v. R* (1934), 99
- Burrows, Andrew
 - contributory negligence, 584, 585
 - cost of cure, 203
 - damages, 524, 526, 556, 570
 - distinction between common law and equity, 12
 - duress, 308, 318
 - injunctions, 537
 - interpretation of written contracts, 387, 401
 - liquidated damages, 609, 610
 - mitigation principle, 580
 - offer and acceptance, 56
 - restitution, 23, 594
 - Rice* case, 498
 - specific performance, 531, 532, 536
 - third party rights, 212
 - unilateral errors, 413
- Burton J
 - Durham v. BAI (Run Off) Ltd* (2008), 166–7
 - M & J Polymers Ltd v. Imerys Minerals Ltd* (2008), 605, 606
 - Stocznia Gdynia SA v. Gearbulk Holdings Ltd* (2009), 480
- business efficacy test, 354, 361–4, 365, 371, 479
 - assessment of, 363–4
 - illustrations, 362–3
- Buxton LJ, 590
 - Irvani v. Irvani* (2000), 337, 338
 - Murray v. Leisureplay plc* (2005), 606
- Cairns LC, Lord
 - Bolton v. Mahadeva* (1972), 515
 - Cundy v. Lindsay* (1878), 297, 303
 - Hughes v. Metropolitan Railway* (1871), 154
- Cantley J, *Bacon v. Cooper (Metals) Ltd* (1982), 400–2, 581
- Capper, D., 322, 335, 336, 337
- Cardozo, Benjamin, 391
- Carnwath LJ
 - KPMG LLP v. Network Rail Infrastructure Ltd*, 402
 - Midill (97PL) Ltd v. Park Lane Estates Ltd and Gomba International* (2008), 615–16
- Cartwright, J., 241, 243, 669
- certainty, 8, 79, 89–113, 252, 664
 - and agreements already substantially settled, 92
 - compromise agreements, 110
 - contracts for regular supply of goods, 101–4
 - and courts' regulation of parties' entitlements and obligations, 94–5
 - establishing price in contracts for the sale of goods, 98–110
 - parties manifesting an intention to displace a contract provision, 104–10
 - substantial dealings for regular supply of goods, 101–4
 - and freedom of contract, 90

- and the intent to create legal relations, 90, 96–8
- and the need for objective guidelines for adjudication, 91–2
- negotiation exclusively reserved to the parties, 111
- no specific performance of vague clauses, 112–13
- objective criteria for recognition of contractual rights, 93–6
- and parties' right to determine the agreement, 92
- and supposed agreements already partly performed, 92
- third party resolution of terms, 111–12
- Chadwick LJ
 - BCCI v. Ali* (2000), 86
 - EA Grimstead & Son Ltd v. McGarrigan* (1988–99), 267
 - Euro London Appointments Ltd v. Claessens International Ltd* (2006), 605
 - Peekay Intermark Ltd v. Australia and New Zealand Banking Group Ltd* (2006), 268
 - Watford Electronics v. Sanderson CFL Ltd* (2001), 267, 268, 269, 433–4
 - WWF-World Wide Fund for Nature v. World Wrestling Federation Entertainment Inc.* ('No. 2') (2007), 593–4
- Chen-Wishart, M., 498
- Cheshire, Fifoot and Furmston, 56
- Chin, N. Y., 312, 324
- civil law jurisdictions, 20, 126, 396, 660
- Civil Procedure Rules, 34, 52, 393, 666
- Clark J, *Thames Valley Power Ltd v. Total Gas & Power Ltd* (2005), 35
- Clarke, Christopher J
 - Birmingham City v. Forde* (2009), 131, 143
 - British Steel Corporation v. Cleveland Bridge and Engineering Co.* (1984), 106–8
 - RTS Flexible Systems Ltd v. Molkerei Alois Müller GmbH* (2009), 105, 106
- Clarke MR, Sir Anthony (now Lord Clarke)
 - Assicurazioni Generali SpA v. Arab Insurance Group (BSC)* (2003), 246, 247, 272
 - Associated British Ports v. Ferryways NV* (2009), 180, 348
 - Dolphin Maritime & Aviation Services Ltd v. Sveriges Angfartygs Assurans Foening* (2009), 209
 - Mediterranean Salvage & Towage Ltd case* (2009), 372, 373
 - Platform Funding Ltd v. Bank of Scotland plc* (2008), 483
 - RTS Flexible Systems Ltd v. Molkerei Alois Müller GmbH* (2009), 43–4
- Clauson J, *With v. O'Flanagan* (1936), 242, 244
- Clive, Eric, 398, 655
- Clyde, Lord
 - Panatown case* (2001), 201, 202
 - Royal Bank of Scotland v. Etridge (No. 2)* (2002), 325
- Cockburn J, *Frost v. Knight* (1872), 486
- codification, 665–72
 - nature and benefits of, 665–6
- Coke, Lord, *Pinnel's Case* (1602), 149
- Collins, Hugh, 14, 651, 663, 665
- Collins LJ, Lawrence
 - Chartbrook Ltd v. Persimmon Homes Ltd* (2009), 396, 397, 399
 - Conlon v. Simms* (2006), 272
 - James Hay case* (2005), 412
 - Michael Wilson & Partners Ltd v. Emmott* (2008), 358
 - Sigma case*, 393–4
- Colman J
 - Cable & Wireless plc v. IBM UK* (2002), 29, 34, 348, 595–6
 - JSC Zestafoni G Nikoladze Ferroalloy Plant v. Ronly Holdings Ltd* (2004) 5, 51
 - Lordsvale case*, 608
 - Nisshin Shipping Co. Ltd v. Cleaves & Co. Ltd* (2004), 197, 208, 216
 - South Caribbean Trading v. Trafigura Beheer BV* (2004), 146
- Commercial Court, 671
- Common Frame of Reference*, 4
- common law, 669
 - assumption of responsibility, 258
 - codification of, 667–8
 - consideration, 126
 - decision-making process, 668
 - doctrines of
 - consideration, 13
 - duress, 12
 - illegality, 621
 - mistake, 12
 - non est factum*, 315
 - dominance of case law, 669–70
 - and equity, 12–13
 - and exclusion clauses, 217–18, 419–20, 425–6
 - fundamental mistake, 279, 294–5
 - international code of, 671
 - joint promisees, 194–5
 - penalty doctrine, 601–11
 - privity of contract, 190–4

- common law (*cont.*)
 - remedies for breach of contract, 12
 - account of profits, 12
 - injunctions, 12
 - specific performance, 12
 - right to terminate for repudiatory breach, 480
 - rules of, 13
 - shared mistake, 280–8
- conditional fee agreements, 636
- confidentiality, 358
- consideration, 8, 117–69, 654
 - adequacy of, 130–1
 - child maintenance cases, 135–7
 - compromises, 131
 - decreasing pacts, 119, 138
 - accelerated payment, 149
 - accelerated payment at creditor's request, 149
 - Common law rule on, 146–53
 - debt is disputed in good faith, 150
 - fresh consideration, 149–50, 151
 - interim or final, 138
 - objections to the common law rule, 147–9
 - part-payment by a third party, 149–50
 - part-payment by cheque, 150–1
 - practical benefits, 147
 - promissory estoppel, 153–62
 - proprietary estoppel, 162–5
 - summary, 161–2
 - waiver and forbearance, 153
 - doctrine of, 125–9
 - functions of, 126, 127
 - elements of, 129–31
 - formality, 121–5
 - function of, 192
 - gratuitous promises to reduce the level of a
 - debt, 119
 - position in equity, 119
 - increasing pacts, 118, 119, 138, 139–46
 - interim or final, 138
 - practical benefits, 142–6
 - and intent to create legal relations, 183
 - and 'just price', 117, 131
 - liability in tort for negligence, 127–9
 - 'marriage consideration', 127
 - nature of, 117
 - past consideration, 118, 131–3
 - pre-existing duty owed to a third party, 118, 137
 - pre-existing statutory or public duty, 118, 133–7
 - promises to pay more for the same performance, 119
 - reliance, 158
 - in the 'soft law' codes, 654
 - sufficient reliance, 158
 - and the variation of contract, 138–9
 - and variation of contracts, 118
- Contract Code (draft), 667
- contract law, 13
 - accessibility in a global market, 670–2
 - assignment, 225–32
 - breach of contract, 8, 127, 253, 475–515
 - consensual remedies, 599–617
 - judicial remedies, 519–97
 - certainty, 8, 79, 89–113, 341
 - characteristics of English, 3–6
 - common law and equity, 12–13
 - consideration, 8, 117–69
 - contexts where statute and common law
 - intertwine, 666
 - contexts where statute predominates, 666
 - doctrines of, 10, 664
 - breach of contract, 8
 - frustration, 9
 - implied terms, 8
 - mistake, 8
 - privity of contract, 9
 - substantial performance, 514
 - dominance of case law, 666
 - problems with the case law technique, 668–9
 - duress, undue influence and unconscionability, 307–41
 - estoppel, 117–69
 - and EU law, 14, 438, 670
 - exclusion clauses, 419–42
 - exercise of reasonable care, 10
 - freedom of contract, 6–7
 - frustration, 9, 445–73
 - and good faith, 13–14
 - illegality and public policy, 621–45
 - implied terms, 353–77
 - intent to create legal relations, 8, 171–84
 - interpretation and rectification of written
 - contracts, 379–417
 - misrepresentation, 235–73
 - mistake, 8, 275–304
 - the objective principle, 7
 - offer and acceptance, 8, 37–87
 - precision of, 5
 - pre-contractual phase, 19–35
 - predictability, 79, 317, 664
 - principles of, 4
 - privity of contract, 188
 - and restitution, 11–12
 - rules and principles, 4

- distinction between, 5
- exceptions, 4
- and the 'soft law' codes, 652–9
- stability of, 291
- and supra-national courts, 665
 - terms, 345–51
 - and third parties, 187–223
- and tort law, 569–70
- contracts
 - acceleration clauses, 608
 - agreements 'subject to contract', 8, 174, 347–8
 - ancillary agreements or clauses, 347–51
 - ancillary negotiation obligations, 32–3
 - arbitration clauses, 99, 101, 215–16, 264, 349, 351
 - bilateral, 7
 - breach of contract, 8, 12, 475–515, 519–97
 - causes of action, 11
 - choice-of-law clauses, 348, 671
 - codification of, 665–72
 - collateral warranties, 347
 - commercial context, 481
 - condition subsequent clauses, 10
 - conditions precedent, 8
 - and conduct subsequent to formation, 386–8
 - consumer contracts, 341
 - defective performance, 9
 - employment contracts, 206, 532, 575, 637
 - entire agreement clauses, 252, 267, 347
 - exclusion clauses, 187, 190, 194, 264, 347, 419–42
 - and the Misrepresentation Act 1967, 265–70
 - exclusive jurisdiction clauses, 220, 223
 - exclusivity agreements, 26–7
 - exemption clauses, 208
 - family financial contracts, 177
 - force majeure* clauses, 347, 446
 - formalities, 121–5
 - formation of, 42–50, 121
 - Himalaya* clauses, 218–20
 - hybrid arbitration and jurisdiction clauses, 351
 - illegality, 621–45
 - implied terms, 8, 346–7, 353–77
 - and international transport conventions, 206
 - invalidation because of duress, undue influence or unconscionability, 308
 - invalidity, 406
 - jurisdiction clauses, 264, 348, 349–50
 - in the EU or Lugano Jurisdictional Zone, 350
 - letters of comfort, 171, 180, 347–8
 - limitation clauses, 11, 434, 609
 - liquidated damages clauses, 264, 599, 605, 609
 - mediation agreements, 32, 124–5, 348
 - mediation clauses, 25
 - modes of ending, 264–5
 - non-exclusive jurisdiction clauses, 220–1
 - non-performance, 9
 - non-reliance clauses, 266, 267, 347
 - consensual basis of, 268
 - non-consensual basis of, 267–8
 - and statutory control, 268–9
 - novation, 231
 - for personal services, 520
 - pre-contractual phase, 19–35, 386
 - prohibitory clauses, 225
 - rescission *ab initio*, 12, 485, 510–13
 - for the regular supply of goods, 101–4
 - repeat transactions, 49
 - rights and obligations of third parties, 9
 - termination clauses, 497
 - termination of, 10
 - terms, 345–51
 - for transfer of movable property, 520, 531
 - unilateral, 7, 39
 - acceptance in, 66–70
 - offer and acceptance, 49
 - vague, 96–8
 - variations to, 9, 121, 152–3, 193
 - voidable, 8
 - written, 8, 122, 303–4, 371–3
 - exceptional situations where a written contract is required, 123
 - interpretation and rectification, 379–417
- contractual rights, objective criteria for recognition of, 93–5
- contributory negligence, 23, 260, 556, 582–6
- Cooke, Sir Robin, 27, 28
- Coote, B., 194, 573
- Corbin, A. L., 196
- Coulson J, *Jani-King (GB) Ltd v. Pula Enterprises Ltd* (2007), 376
- Cross, Lord, *Barton v. Armstrong* (1976), 315
- culpa in contrahendo*, 20
- Cumming-Bruce LJ, *Staffordshire Area Health Authority v. South Staffordshire Waterworks Co.* (1978), 482
- damages, 210
 - capital loss, 253
 - and compensation, 550, 551–2
 - 'consumer surplus' measure of, 524–52
 - in employment disputes, 552
 - compensatory, 519, 602

damages (*cont.*)

- consequential loss, 253, 263
- contractual and tort damages, 552–3
- contributory negligence
 - and breach of contract, 584–5
 - reform of the law on, 584–5
- cost of cure, 263, 545–6
 - and the mitigation principle, 581–2
 - Radford v. De Froberville* (1977), 546
 - Tito v. Waddell* (No. 2) (1977), 546–9
- economic interests
 - expectation interest, 544
 - reliance interest, 544
 - restitutionary interest, 544
- extravagant and unconscionable, 599
- foresight and contemplation, 658
- limiting factors
 - causation, 542, 554–5
 - contributory negligence, 542
 - defendant's choice or discretion in performing contract, 543
 - impecuniosity, 542
 - litigation costs and damages, 542–3
 - mitigation, 542
 - remoteness, 542, 556–70
 - scope of duty test, 570–2
- limits on damages claims, 554–86
- liquidated damages, 599–617
 - attractions of, 601
 - and the penalty doctrine, 601–11
 - punishment is not the aim, 611
- loss of bargain damages, 253
- loss of chance claims, 550–1
- mitigation principle, 573–82
 - application of, 577, 582
 - and claims for debt, 582
 - and contributory negligence, 582–6
 - and cost of cure damages, 581–2
 - duty to endeavour to reduce or eliminate loss, 574–7
 - examples, 575–6
 - mitigation in face of hazardous breach, 577–8
 - mitigation in fact achieved, 579–81
 - recovery of extra loss for attempt to mitigate, 578–9
 - sale of goods, 575–7
 - wrongful dismissal, 575
- in non-English codes, 558
- penalty doctrine, 601–11
 - acceleration clauses, 608
 - attractions of, 601
 - breach triggering liability, 603–4

- commercial parties, 605–6
- consequence of finding a penalty, 608–9
- critique of, 610–11
- date of assessment, 603
- equality of bargaining power, 606
- fundamental statement of, 601–3
- invalid liquidated damages clause not a cap, 609–10
- need for breach as between payor and payee, 604–5
- 'no deterrent purpose' test, 606–7
- objective test, 603
- penalty in the context of money obligations, 607–8
- rejoinder to the critique, 611
- single sum payable, 607
- types of clauses covered by, 605
- valid liquidated damages clause acts as a cap, 609
- reliance loss claims, 519, 545
- remoteness
 - cases on, 568–70
 - ordinary course of things, 569
 - overlapping claims in tort and contract, 569–70
 - in the 'soft law' codes, 657–9
 - and 'scope of duty' tests, 566–8
 - special information, 569
- in the 'soft law' codes, 657, 658, 659
- tort claims for loss of business opportunities, 552–3
 - protected expectations, 553
 - warranted expectations, 553
- types of claims, 544–54
 - expectation and reliance loss claims, 544–5
 - to reflect post-breach events, 572–3
- unusual loss consequent on delayed or interrupted supply of goods or services, 557–8
- 'windfall' damages, 549–50

Danckwerts LJ

- D & C Builders v. Rees* (1966), 150, 157
- Jones v. Padavatton* (1969), 178

Davenport, Brian, 513

- deceit, 11, 246, 253–6, 553–4, 641
- deeds, 8, 121, 295–6

Denning MR, Lord

- Alan v. El Nasr* (1972), 153
- Amalgamated Investment & Property Co. Ltd v. Texas Commerce International Bank Ltd* (1982), 387–8, 400
- Ashmore, Benson, Pease & Co Ltd v. AV Dawson Ltd* (1973), 640

- Beswick v. Beswick* (1968), 192
Butler Machine Tool Co. Ltd v. Ex-Cell-O Corporation (England) Ltd (1979), 60–2
Charles Rickards Ltd v. Oppenheim (1950), 152
Combe v. Combe (1951), 129, 159
D & C Builders v. Rees (1966), 151, 162, 320–1
Enderby Town FC Ltd v. Football Association (1971), 630
Entores Ltd v. Miles Far East Corporation (1955), 44–5
Errington v. Errington & Woods (1952), 69, 70
‘*The Eugenia*’ (1964), 377, 450, 453, 457
Federal Commerce & Navigation Co. v. Molena Alpha Inc. (1979), 489
fundamental breach doctrine, 426
Gibson v. Manchester CC (1979), 42
Gould v. Gould (1970), 173
H Parsons (Livestock) Ltd v. Uttley Ingham & Co. Ltd (1978), 563
‘*The Hansa Nord*’ (1976), 500
High Trees case (1947), 119, 154–5, 156
Howard Marine and Dredging Co. Ltd v. A. Ogden & Sons (Excavations) Ltd (1978), 249, 258
inequality of bargaining power, 340
Lloyd’s Bank v. Bundy (1975), 308, 325–6, 340
Morris v. C W Martin & Sons Ltd (1966), 223
Rose v. Pim (1953), 410
Schuler (L) AG v. Wickman Machine Tool Sales Ltd (1974), 493–4
Scruttons v. Midland Silicones (1962), 217
shared mistake, 291
Solle v. Butcher (1950), 289, 290, 293, 300
Staffordshire Area Health Authority v. South Staffordshire Waterworks Co. (1978), 482
Stockloser v. Johnson (1954), 612
Ward v. Byham (1956), 135, 136
Williams v. Williams (1957), 135, 136–7
dependence, relationships of, 329
deposits, 612–17
 common law jurisdiction to control excessive deposits, 616–17
 compensation over and above the amount of the deposit, 613
 customary levels, 616
 failure to pay, 614
 forfeiture of, 613
 sources of relief, 614–16
 statutory relief to order repayment in context of land transactions, 614
Devlin, Lord, 310
 Heaven & Kesterton Ltd v. Etablissements Francois Albiac et Cie (1956), 575
 Hedley Byrne & Co. v. Heller (1964), 128
 Ingram case (1961), 300–1
 Parker v. Clark (1960), 173, 178–9
 St John Shipping Corporation v. Joseph Rank Ltd (1957), 629
 Universal Cargo Carriers Corporation v. Citati (1957), 485, 486
Dilhorne, Viscount, *New Zealand Shipping v. Satterthwaite* (‘*The Eurymedon*’) (1975), 219
Dillon LJ
 Johnson v. Johnson (1989), 601–3
 ‘*The Super Servant Two*’ (1990), 465
Diplock, Lord
 Antaios Cia Naviera SA v. Salen Rederierna AB (1985), 388, 390, 498–9
 Gibson v. Manchester CC (1979), 42
 ‘*The Hannah Blumenthal*’ (1983), 78
 Harvela v. Royal Trust Co. of Canada (1986), 76
 Hongkong Fir case (1962), 493, 500, 501
 Photo Production Ltd v. Securicor Transport Ltd (1980), 426
 Pioneer Shipping Ltd v. BTP Tioxide Ltd (‘*The Nema*’) (1982), 384
 Robophone case (1996), 610
dispute resolution, adjudicative standards for, 91
Donaldson QC, David, *Adam Opel GmbH v. Mitras Automotive UL Ltd* (2008), 320
Draft Common Frame of Reference, 650
Dubai International Financial Centre, 65, 126, 397, 667, 668
Duke LJ, *Balfour v. Balfour* (1919), 176
Dunedin, Lord
 Dunlop Pneumatic Tyre Co. v. New Garage and Motor Co. Ltd (1915), 601–2, 607
 Dunlop Pneumatic Tyre Co. Ltd v. Selfridge & Co. Ltd (1915), 125, 193
 May & Butcher v. R (1934), 99
duress, 307, 308; see also undue influence, unconscionability
 components of, 310–11
 causal impact of the pressure, 314–15
 implicit or overt pressure, 311
 improper nature of the threat, 312–13
 lawful threat or pressure, 313
 objective potency of pressure, 314
 R v. Her Majesty’s Attorney-General for England and Wales (2003), 313–14
 target of threat and maker of the threat, 312
 unlawful threat or pressure, 312
and contractual consent, 310, 315
‘decisive influence’ test, 314
and decreasing pacts, 320–1

- duress (*cont.*)
 - defence of affirmation, 316
 - nature of contractual invalidity, 315–16
 - predictability of the law, 317
 - and procedural unfairness, 339
 - and renegotiation of contracts, 316–18
 - commercial pressure and renegotiated agreements, 320
 - commercial pressure during, 319–20
 - ways in which it can occur, 316
 - substantially unfair bargain, 318
- Dyson J
 - Crossley v. Faithful & Gould Holdings Ltd* (2004), 357, 361
 - DSND Subsea Ltd v. Petroleum Geo-Services ASA* (2000), 312, 317
 - Paragon Finance plc v. Nash* (2002), 369
 - Tekdata Intercommunications v. Ampenol Ltd* (2009), 62–3
- Edmund-Davies J, *Wells (Mertsham) v. Buckland Sand & Silica Ltd* (1965), 252
- Ellenborough, Lord, *Stilk v. Myrick* (1809), 141
- equity
 - and common law, 12–13
 - doctrines of
 - bars upon rescission, 12
 - rectification, 12, 277, 382, 402
 - rescission for shared mistake, 288
 - shared mistake, 276
 - unconscionability, 12
 - undue influence, 12
 - equitable penalty rule, 340
 - Supreme Court of Judicature Acts 1873 and 1875, 12
- Esher, Lord
 - '*The Moorcock*' (1889), 362
 - Nottingham Patent Brick & Tile Co. Ltd v. Butler* (1886), 239
- estoppel, 117–69
 - by convention, 165–7, 168, 387, 400, 402
 - and rectification, 409
 - promissory estoppel, 119, 120, 139, 147, 153–62, 166, 168, 183, 320
 - elements of, 153–4
 - not a cause of action, 159–61, 162
 - suspension/extinction debate, 154–9
 - proprietary estoppel, 120, 159, 160, 161, 162–5, 166, 168
 - limited to situations relating to land, 165
 - and remedial discretion, 163
 - by representation, 121, 161, 162, 165, 166, 167
 - res judicata*, 168–9
 - and 'subject to contract', 174
 - types of, 167–9
- European Code of Private law, 665
- European Court of Justice, 349, 350, 650
- European Union law, 14, 438, 670
 - civil code, 650, 651
- Consumer Protection from Unfair Trading Regulations 2008, 14
- consumer protection legislation, 425
- draft European Code of Contracts, 650
- EU Directive on Unfair Commercial Practices, 14
- and jurisdiction and arbitration clauses, 349
- and Unfair Terms in Consumer Contracts Regulations 1999, 14
- ex turpi causa non actio oritur*, 621, 625, 626
- exclusion clauses
 - and the Consumer Contracts Regulations 1999, 437–42
 - and fraud, 425
 - incorporation of, 419, 420–4
 - based on trade usage, 424
 - case law on, 421–4
 - the clause is in a document with apparent contractual force, 424
 - by a consistent course of dealing between the parties, 424
 - signature effective for, 422–3
 - the test, 420–2
 - interpretation of *contra proferentem*, 425
 - and liability for fraud, 419
 - and the Misrepresentation Act 1967, 426–7
 - notice, 419
 - principles of construction, 425
 - and statutes, 420
 - strict interpretation at common law, 425–6
 - respect for clear wording, 426
 - types of, 419
- and the Unfair Contract Terms Act 1977, 427–37
 - business-to-business dealings, 434
 - case law on, 433–7
 - reasonableness test, 434
- and the Unfair Terms in Consumer Contracts Regulations, 437–42
- exploitation. *see* unconscionability
- fair dealing, 20, 72, 375
- fairness, subjective and objective determination of, 28
- Fauvaraque-Cosson, Bénédicte, 650
- Feltham, J. D., 195

- Fenton-Atkinson LJ, *Jones v. Padavatton* (1969), 178
- fiduciary duties, 273, 588, 591
- Flaux J, *ASM Shipping Ltd of India v. TTME Ltd of England* ('The Amer Energy') (2009), 566
- Flaux QC, Judge Julian, *Rhodia International Holdings Ltd v. Huntsman International LLC* (2007), 30
- foreseeability, 452–4, 558
in the 'soft law' codes, 658
- formality, 120, 121–5
in land transactions, 123–4
mediation agreements, 124–5
- France
interpretation of written contracts, 398
Code Civil, 611
- Fraser, Lord, *Sudbrook Trading Estate Ltd v. Eggleton* (1983), 111–12
- fraud
equitable fraud, 326
and exclusion clauses, 425
- freedom of contract, 6–7, 19, 90, 92, 111, 173, 174, 221
and assignment, 226
elements of, 6
limitations on, 6–7
qualifications upon, 221–2
- frustration, 9, 445–73
allocation of the risk, 451–2
and breach of contract, 512
consequences of, 467–72
default and self-induced frustration, 463–6
choice precludes frustration, 464
short supply and too many customers, 466
- doctrine of
allocation of the risk, 446
and default, 446
definition and genesis of the doctrine, 447–9
and *force majeure* clauses, 446, 457, 466
foreseeability and risk allocation, 452–4
history of the doctrine, 448–9
situations giving rise to, 445–6
and implied terms, 377, 449–50
and mistake, 450–1
by operation of law, 464
- PECL, *Principles of European Contract Law*, 457–8, 487
- and restitution, 587
- scope of, 454–63
delay, 459–61
difficulty and 'impracticability', 455–8
exceptional source of, 461–2
insufficient delay, 460
leases, 462–3
physical impossibility, 455
successful plea, 459
sufficient delay, 460–1
supply of generic goods, 458–9
and the 'soft law' codes, 655
strict interpretation at common law, 457
supervening illegality, 454–5
termination of contracts of indefinite duration, 472–3
UNIDROIT *Principles of International Commercial Contracts*, 458
- Garland J, *Gamerco SA v. JCM/Fair Warning (Agency) Ltd* (1995), 468–9
- Gatehouse J, *Schelde Delta Shipping BV v. Astarte Shipping BV* ('The Pamela') (1995), 46
- Gendolfi, Giuseppe, 650
- Gibson LJ, Peter
Gardner v. Marsh & Parsons (a firm) (1997), 581
Re Selectmove (1995), 49
Swainland Builders Ltd v. Freehold Properties Ltd (2002), 409
- Gifford, Lord, 395
- Glidewell LJ, *Williams v. Roffey & Nicholls (Contractors)* (1991), 143
- Gloster J
JP Morgan Chase v. Springwell Navigation Corp (2008), 422, 434
Shell Egypt West Manzala GmbH v. Dana Gas Egypt Ltd (2009), 351
Six Continental Hotels case (2006), 267, 269, 270
- Goff (Reginald) LJ, *Daulia v. Four Millbank Nominees* (1978), 69
- Goff (Robert) J
British Steel Corporation v. Cleveland Bridge and Engineering Co. (1984), 587
The Post Chaser (1982), 158
- Goff (Robert) LJ
Allied Marine Transport Ltd v. Vale do Rio Doce Navigacao SA ('The Leonidas D') (1985), 48
Amalgamated Investment & Property Co. Ltd v. Texas Commerce International Bank Ltd (1981), 161
Beer v. Bowden (1981), 102
BP Exploration Co. (Libya) Ltd v. Hunt (No. 2) (1979), 467, 470, 471
British Steel Corporation v. Cleveland Bridge and Engineering Co. (1984), 21–3
Staffordshire Area Health Authority v. South Staffordshire Waterworks Co. (1978), 482

- Goff (Robert), Lord
Dimskal Shipping Co. SA v. ITWF ('The Evia Luck No. 2') (1992), 311
'The Kanchenjunga' (1990), 508
'The Mahkutai' (1996), 220
Panatown case (2001), 204
 good faith, 13–14, 20, 28–30, 355
 agreement to negotiate in, 24, 31–2, 33–4
 and exclusion clauses, 440
 and implied terms, 375–7
 judicial decisions on, 661–2
 post-formation, 664–5
 and rectification, 416
 in the 'soft law' codes, 653, 659–65
 in tendering, 73
 Goudge JA, *Miller Paving Ltd v. B Gorrardo Construction Ltd* (2007), 291
 Goulding J
 Patel v. Ali (1984), 473
 Sky Petroleum v. VIP Petroleum Ltd (1974), 531
 Griffiths, Lord
 Linden Gardens Trust Ltd v. Lenesta Sludge Disposals Ltd (St Martins Property Corporation Ltd v. Sir Robert McAlpine Ltd) (1994), 202–3, 205
 guarantees, 8
 Hague-Visby rules, 219, 220
 Haldane LC, Viscount
 British Westinghouse case (1912), 573, 579
 Dunlop Pneumatic Tyre Co. Ltd v. Selfridge & Co. Ltd (1915, 1.11), 191–2
 Hale, Baroness
 Macklin v. Dowsett (2004), 633
 MacLeod v. MacLeod (2008), 177, 633
 Rice v. Great Yarmouth BC (2000), 505
 Transfield Shipping Inc. v. Mercator ('The Achilleas') (2008), 564, 565–6, 571
 Halson, R., 318, 610
 Hamilton J, *Easton v. Hitchcock* (1912), 362
 Hardwicke LC, Lord, *Tomlinson v. Gill* (1756), 195
 Harman J, *Pilkington v. Wood* (1953), 574
 Hedley, Steve, 3
 Herschell, Lord
 Derry v. Peek (1889), 253–4
 Grainger & Sons v. Gough (1896), 40
 Hewart CJ, Lord
 Foley v. Classique Coaches (1934), 102
 Maple Flock Co. Ltd v. Universal Furniture Products (Wembley) Ltd (1934), 497
Himalaya clauses, 218–20
 Hirst J
 Anangel Atlas Compania Naviera SA v. Ishikawajima Harima Heavy Industries Co. Ltd (No. 2) (1990), 146
 Kleinwort Benson v. Malaysian Mining (1989), 181
 Hobhouse, Lord, 650–1
 Attorney-General v. Blake (2001), 590, 592
 Reeves v. Commissioner for Metropolitan Police (2000), 248
 Royal Bank of Scotland v. Etridge (No. 2) (2002), 322, 325, 327
 Shogun Finance Co. Ltd v. Hudson (2003), 299, 303, 406–7
 Vesta case (1989), 582–3
 Hodson, Lord
 Ajayi v. Briscoe (1964), 155, 158
 C Czarnikow Ltd v. Koufos ('The Heron II') (1969), 561
 Hoffmann, Lord, 393
 Attorney-General for Belize v. Belize Telecom Ltd (2009), 354–5, 366, 367, 371–3
 Banque Bruxelles Lambert SA v. Eagle Star Insurance Co. Ltd (the 'SAAMCO' case) (1997), 570, 572
 BCCI v. Ali (2002), 85, 271, 293, 393
 C Czarnikow Ltd v. Koufos ('The Heron II') (1969) L, 562
 Carmichael v. National Power plc (1999), 384, 385, 387
 Chartbrook Ltd v. Persimmon Homes Ltd (2009), 395, 396, 397–8, 399–400, 401, 402, 403, 407, 408, 409
 Co-operative Insurance Services v. Argyll Stores Ltd (1998), 532, 534, 535–6, 537
 Gray v. Thames Trains Ltd (2009), 625
 Investors Compensation Scheme Ltd v. West Bromwich Building Society (1998), 380, 388–90, 394
 OBG Ltd v. Allan (2007), 221–2
 Pratt Contractors Ltd v. Transit New Zealand (2003), 75
 Premium Nafta Products Ltd v. Fili Shipping Co. Ltd (2007), 100–1
 R v. Her Majesty's Attorney-General for England and Wales (2003) 4, 322
 South Australia Asset Management Corp v. York Montague Ltd (1997), 567
 Transfield Shipping Inc. v. Mercator ('The Achilleas') (2008), 561, 564, 565, 567, 568, 571

- Union Eagle Ltd v. Golden Achievement Ltd* (1997), 507
- William Sindall plc v. Cambridgeshire CC* (1994), 451
- Hudson, A. H., 56
- Ibbetson, D., 448
- illegality (and public policy), 621–45
- agreements expressly or impliedly prohibited by statute, 628–9, 640
 - agreements to commit a legal wrong, 627, 640
 - claimant's association with the unlawful activity, 639–40
 - claimant's participation in unlawful performance, 639–40
 - consequences of, 622–3, 645
 - claim for a *quantum meruit*, 641
 - recovery of property, 641
 - restitution, 643–5
 - textual severance of an illegal part of a written contract, 642
 - tort of deceit, 641
 - transfer of property, 641
 - factors the court might consider, 624
 - gambling contracts, 629–30
 - policies underlying, 623, 625
 - rights of the innocent party, 639
- implied terms, 8, 346–7, 353–77
- and complex commercial agreements, 370–1
 - custom or trade usage
 - continuity of acts, 374
 - criteria for recognition, 373–4
 - and frustration, 377
 - and good faith, 355, 375–7
 - and interpretation of written contracts, 407
 - and mistake, 377
 - PECL, *Principles of European Contract Law*, 355
 - and rectification, 409
 - terms implied in fact, 353–5, 361–73
 - business efficacy test, 354, 361–4, 365, 371
 - contamination of 'policy factors', 366–7
 - criteria for finding, 361
 - custom or trade usage, 355, 373–4
 - financial services cases, 367–8
 - lender's terms, 368–70
 - Moorcock* test, 354
 - need for restraint, 354
 - objective bystander test, 364, 370
 - offer and acceptance, 368, 371
 - officious bystander test, 354, 364–6, 372
 - terms implied in law, 353, 356–61, 367
 - arbitration, 358
 - confidentiality, 358
 - contractual duty of care, 358
 - damaging the future prospects of employees, 359–60
 - employment cases, 358–61
 - judicial precedent, 354
 - Liverpool City Council v. Irwin*, 357
 - overworking young doctors, 359
 - pensions, 360–1
 - and the tort of negligence, 374–5
- UNIDROIT *Principles of International Commercial Contracts*, 355
- and written contracts, 371–3
- independent legal advice, 333–4
- injunctions, 12, 537–9
- intent to create legal relations, 8, 126, 171–84, 633
- borderline of commercial and non-commercial contexts, 182
 - Modahl v. British Athletic Federation Ltd* (2002), 182–3
 - and certainty, 90, 96–8, 184
 - collective agreements, 174
 - in commercial contexts, 171, 173, 179–82
 - discovering 'intent', 173
 - and enforceability, 175
 - foundations of the doctrine, 172–5
 - and freedom of contract, 173, 174
 - and 'gentlemen's agreements', 173
 - letters of comfort, 171, 180, 347–8
 - in non-commercial contexts, 172, 173, 175–9
 - bargains between spouses, 175–7
 - friends sharing accommodation, 178–9
 - other family arrangements, 177–8
 - and offer and acceptance, 172
 - practical and policy factors, 172, 175
 - rationale for the doctrine, 173–5
 - status of, 183–4
 - and consideration, 183
 - and offer and acceptance, 184
 - 'subject to contract', 171, 174
- interpretation and rectification of written contracts, 379–417
- to eliminate obvious errors, 401–4
 - and implied terms, 407
 - and the parol evidence rule, 405–7
 - pre-contractual negotiations for, 394–401
 - rectification, 407–17
 - rules governing, 385–94
 - in the 'soft law' codes, 655–6
 - written contracts and questions of 'law', 383–5

- Irvine LC, Lord, *Carmichael v. National Power plc* (1999), 384
- Jack, Judge Raymond, *Government of Zanzibar case* (2000), 268, 270
- Jack J, *Carleton v. Strutt & Parker* (2008), 35
- Jackson J, *Alfred McAlpine Capital Projects v. Tilebox Ltd* (2005), 603, 605, 636
- Jackson QC, Rupert, *Williams v. Roffey & Nicholls (Contractors)* (1991), 142
- Jacob LJ
IRC v. Fry (2001), 150
Jeancharm Ltd v. Barnet Football Club Ltd (2003), 606
R Griggs Group v. Evans (No. 1) (2005), 366
Thomas Witter Ltd v. TBP Industries Ltd (1996), 270
- Jauncey, Lord
Panatown case (2001), 201, 202
Ruxley Electronics Ltd v. Forsyth (1996), 547
- Jessel MR, *Redgrave v. Hurd* (1881), 237
- Jones, Gareth, 515
- judicial remedies for breach of contract, 519–97
 action for debt, 519, 523–30
 assessment of the 'legitimate interest' criterion, 528–30
 case law development of the co-operation qualification, 525
 legitimate interest test, 525, 526–30
 'no legitimate interest' cases, 527
 penalty doctrine, 524
 'performer enjoying a legitimate interest' cases, 528
 damages, 519–20, 586
 agreed compensation, 540
 assessed at date of breach, 541
 causation, 542
 finality, 542
 limiting factors, 542–3
 limits on damages claims, 554–86
 nominal damages, 540
 protection of expectations and indemnification of reliance loss, 540–1
 purpose of, 541
 remoteness, 542
 substantial damages, 540
 true compensation, 540
 types of money claims, 544
 declarations, 595
 negative declarations, 595
 injunctions, 530, 537–9
 indirect compulsion, 538–9
 mandatory injunctions, 538
 prohibitory relief, 538
 interest on money claims, 596–7
 restitutionary claims. *see* restitution
 specific performance, 530–7
 availability of, 532, 534
 and contempt of court, 530, 536
 Co-operative Insurance Services v. Argyll Stores Ltd (1998), 534–7
 criteria for, 531
 danger of oppression of the defendant, 536
 discretion about, 532
 disproportion between harm to defendant and loss to claimant, 536
 and employment contracts, 532
 equitable remedy of, 535
 mitigation principle, 537
 punishment is not the aim, 535
 scarce goods, 531
 scope of, 537
 supervision of an order and the obligation to achieve a result, 429
 and transfer of land, 536
 stays upon legal proceedings, 595–6
 types of, 519–21
 'account of profits', 12, 520–1, 588
 action for debt, 519
 damages, 519–20
 injunctions, 520
 specific performance, 520
 just price (*iustum pretium*), 117, 131
- Kay LJ, Maurice, *Chief Constable of the Greater Manchester Police v. Wigan AFC* (2008), 134–5
- Kenyon, Lord
Cutter v. Powell (1795), 513
Harris v. Watson (1791), 141
- Kerr LJ
B & S Contracts & Design Ltd v. Victor Green Publications Ltd (1984), 319
Dean v. Ainley (1987), 550
'The Karen Oltmann' (1976), 398–9, 402
'The Odenfeld', 528
'The Siboen and the Sibotre' (1976), 316, 317, 320
- Kilbrandon, Lord, *Schuler (L) AG v. Wickman Machine Tool Sales Ltd* (1974), 495
- Kirby J, *Koomphahtoo Local Aboriginal Land Council v. Sanpine Pty Ltd* (2007), 500
- Latham LJ, *Primavera v. Allied Dunbar Assurance plc* (2002), 580

- Law Commission, 438, 667
 and consideration, 126
 Contracts (Rights of Third Parties) Act 1999, 209, 211, 212
 and contributory negligence, 584
 double compensation, 214
 exclusion of the Act by contracting parties, 215
 firm offer rule, 65
 illegality, 621, 624, 626
 interest on money claims, 597
 privity of contract, 193
 Sale of Goods Act 1979, 502
 third party rights, 187
White v. Jones, 209
- Law Reform Committee
 'fiction of fraud', 257
 mistake, 300–1
- Law Revision Committee, 132
- Lawrence, A. T. J., *Scriven Bros v. Hindley* (1913), 81
- Lawson, F. H., 533
- Lawton LJ
Butler Machine Tool Co. Ltd v. Ex-Cell-O Corporation (England) Ltd (1979), 60
Holwell Securities Ltd v. Hughes (1974), 54–5
- Leggatt LJ, *Johnstone v. Bloomsbury Health Authority* (1992), 375
- Leveson LJ, *Avraamides v. Colwill* (2006), 207
- Lewison J
Re Griffiths, 295
Thompson v. Foy (2009), 321
- Lightman J, 392
Inntreprenuer case (2000), 267
Malcolm v. Chancellor, Masters & Scholars of the University of Oxford (1994), 97
- Lindley LJ
Allcard v. Skinner (1887), 323, 325
Nottingham Patent Brick & Tile Co. Ltd v. Butler (1886), 239
- Liu, Q., 573
- Lloyd Lord
'The Alaskan Trader' (1984), 527
Business Environment Bow Lane Ltd v. Deanwater Estates Ltd (2007), 251
Investors Compensation Scheme Ltd v. West Bromwich Building Society (1998), 389
Reichman v. Beveridge (2006) 525
Ruxley Electronics Ltd v. Forsyth (1996), 540, 547, 548
Stour Valley Builders v. Stuart (2003), 150
- Longmore LJ
Collier v. P & MJ Wright (Holdings) Ltd (2007), 158–9
Devenish Nutrition Ltd v. Sanofi-Anetis SA (2008), 595
Maple Leaf Macro Volatility Master Fund v. Rouvroy (2009), 122–3
Petromec Inc. etc. v. Pertoleo Brasileiro SA (2005), 24, 31–2
Soulsbury v. Soulsbury (2007), 66, 70
 Loreburn, Lord, *Tennants (Lancashire) Ltd v. C S Wilson & Co.* (1917), 456
- Lugano Convention, 349, 350
- Lush J
Currie v. Misa (1875), 125
Easton v. Hitchcock (1912), 362
Horwood v. Millar's Timber and Trading Co., Ltd (1916), 634
Stevenson Jacques & Co. v. McLean (1879), 57–8
- Macdonald, Elizabeth, 318
- MacKinnon LJ
Chapelon v. Barry UDC (1940), 424
Shirlaw v. Southern Foundries (1926) Ltd (1939), 354, 363–4, 368
- MacMillan, Catherine, 285, 290, 300
- Mance, Lord
Baird Textile Holdings Ltd v. Marks & Spencer plc (2001), 181, 184
Charter Reinsurance Co. Ltd v. Fagan (1997), 392, 393
Experience Hendrix LLC v. PPX Enterprises (2003), 591
Friends Provident Life & Pensions Ltd v. Sirius International Insurance Corp (2005), 512
Hall v. Woolston Hall Leisure (2001), 640
Huyton SA v. Peter Cremer GmbH & Co. (2003), 317–18
LauritzenCool AB v. Lady Navigation Inc. (2005), 539
The Office of Fair Trading v. Abbey National plc (2009), 439–40
OT Africa Lines v. Vickers plc (1996), 81, 292–3
Sempre Metals Ltd v. Inland Revenue Commissioners (2007), 1, 557, 597
- Mansfield CJ, *Holman v. Johnson* (1775), 626
- Martin, Sir Andrew V-C, 91
- Martin B, *Pearce v. Brooks* (1866) 668
- May LJ, *Business Environment Bow Lane Ltd v. Deanwater Estates Ltd* (2007), 251
- McGregor, H., 263, 435, 549
- McKendrick, E., 183, 261, 396, 433, 472, 501, 660

- McLaughlan, D. W., 299, 400, 415
- McMeel, G., 382, 406
- McNair J, *Andrews v. Hopkinson* (1957), 252
- mediation agreements, 35, 124–5, 348
- Megarry J
- Cresswell v. Potter* (1978), 336
 - Hounslow LBC v. Twickenham Garden Developments Ltd* (1971), 525
 - Tito v. Waddell (No. 2)* (1977), 546–7
- Megaw LJ
- Alan v. El Nasr* (1972), 153
 - Edwards v. Skyways Ltd* (1964), 179
 - Thornton v. Shoe Lane Parking* (1971), 421
- Mellish LJ, *Parker v. South Eastern Railway Co.* (1877), 421
- Millett, Lord
- Alec Lobb (Garages) Ltd v. Total Oil GB Ltd* (1983), 334, 335–6
 - Allied Maples Group v. Simmons & Simmons* (1995), 551
 - Freeman v. Niroomand* (1996), 548
 - Gibbon v. Mitchell* (1990), 295
 - Hurst v. Bryk* (2002), 512
 - Little v. Courage* (1995), 24, 27
 - National Commercial Bank (Jamaica) Ltd v. Hew* (2003), 331
 - Panatoun case* (2001), 204
 - Shogun Finance Co. Ltd v. Hudson* (2003), 278, 300, 302
 - Taylor v. Bhail* (1996), 642
- misrepresentation, 235–73
- and breach of contract, 510–13
 - and coercion, 331–2
 - collateral warranties
 - and the common law privity problem, 292
 - and the parol evidence rule, 251–2
 - compensation, 235
 - for breach of contract, 253
 - deceit claims and ‘income losses’, 255–6
 - loss of bargain damages, 248, 253
 - under the Misrepresentation Act 1997, 253
 - tort of deceit, 253–6
 - criteria for finding ‘contractual assurances’
 - importance to the representee, 249
 - independent verification, 250
 - need for independent verification negated, 250
 - objective commitment by the maker of the statement, 249
 - obvious importance, 249
 - relative skill, knowledge and expertise of the parties, 250
 - statement of fact versus statement of future fact, 250
 - damages under section 2(1) of the Misrepresentation Act 1967, 256–60
 - deceit and fraud, 256–9
 - defences to Section 2(1) claims, 259–60
 - ‘fiction of fraud’, 257
 - principal liable but not agent, 259
 - duties to disclose, 236, 270–3
 - qualifications, 271
 - elements of, 236–48
 - falsity, 241–2
 - persons involved, 241
 - pre-formation, 241
 - reliance, 242
 - requirement of materiality, 242
 - statement or conduct, 238–41
 - exclusion clauses
 - consensual basis of non-reliance clauses, 268
 - entire agreement clauses, 267
 - and the Misrepresentation Act 1967, 265–70
 - non-consensual basis of non-reliance clauses, 267–8
 - non-reliance clauses, 267
 - non-reliance clauses and statutory control, 268–9
 - potential liability for fraud, 270
 - inducement, 246
 - materiality, 245
 - and mistake, 236, 280
 - reliance, 244–8
 - correction, 247
 - decisive influence, 246–7
 - if the statement is fraudulent, 247–8
 - and inducement, 247
 - need for, 244–5
 - relevance of materiality, 245–6
 - representee can omit to check, 247
 - remedies available, 244
 - damages, 235, 244
 - rescission, 235, 244
 - rescission *ab initio*, 237, 260–3, 512
 - bars to rescission, 262
 - and compensation for breach, 264
 - discretion to withhold, 262–3
 - equitable bars to, 236
 - indemnity, 261
 - non-fraudulent misrepresentation, 262–3
 - and termination for breach, 263–5
 - statements becoming terms or collateral warranties, 248–52

- criteria for finding 'contractual assurances', 249–51
- termination for breach and rescission for misrepresentation, 263–5
- and undue influence, 331–2
- when a statement becomes false before the formation of a contract, 242–4
- criterion of fault, 243
- need for knowledge, 242–3
- strict responsibility, 243
- mistake, 275–304
 - common mistake, 276
 - deeds and 'voluntary instruments', 295–6
 - error as to a party's identity, 276–7, 296–305
 - apportionment, 300–1
 - case law, 298–300, 301–2
 - distance dealings and voidness at common law, 296–8
 - face-to-face dealings, 301, 304
 - rescission by victim of fraud, 301
 - the standard problem, 296
 - summary, 303–5
 - written contracts, 303–5
 - essentially different quality test, 284
 - and frustration, 450–1
 - and implied terms, 377
 - and misrepresentation, 236
 - narrow doctrine of, 279
 - nature of, 278–80
 - need for apparent agreement, 278
 - no rescission for shared mistake in equity, 288–92
 - categories of equitable mistake, 289–92
 - non est factum*: fundamental error in signed documents, 294–5
 - retention of the doctrine, 295
 - operationalisation of, 275
 - and rectification, 408
 - related doctrines, 279–80
 - breach of contract, 279
 - misrepresentation, 280
 - property already owned by purchaser or destroyed before sale, 280
 - shared error as to quality, 280
 - unilateral error as to substance known to the other party, 280
 - shared mistake, 276, 280–8, 655
 - implied term technique, 287–8
 - mistake of law, 286–7
 - res extincta*, 281, 282
 - res sua*, 281, 282
 - in the 'soft law' codes, 655
 - and specific performance, 275, 276
 - types of mistake, 279
 - induced mistake, 279
 - shared mistake, 279
 - unilateral mistake known to the other party, 279
 - unilateral errors, 292–3, 294
- Mocatta J, *'The Atlantic Baron'* (1979), 316
- Moore-Bick LJ
 - ICI Chemical & Polymers Ltd v. TTE Training Ltd* (2007), 383
 - Peckay Intermark Ltd v. Australia and New Zealand Banking Group Ltd* (2006), 268
 - Stocznia Gdynia SA v. Gearbulk Holdings Ltd* (2009), 479, 480–1
- Morgan J, 573
 - Berkeley Community Villages Ltd v. Pullen* (2007), 33, 377
- Morris, Lord
 - C Czarnikow Ltd v. Koufos ('The Heron II')* (1969), 561
 - Société Co-operative Suisse* case (1946), 459
 - Ward v. Byham* (1956), 135
- Morriss, Sir Andrew V-C
 - Business Environment Bow Lane Ltd v. Deanwater Estates Ltd* (2007), 251
 - Equitable Life Assurance Co. Ltd v. Hyman* (2002), 368
 - Esso Petroleum Ltd v. Niad Ltd* (2003), 591
 - Spice Girls Ltd v. Aprilia World Service BV* (2002), 244, 245
- Moss QC, Gabriel, *Internet Broadcasting Corp Ltd v. MAR LLC* (2009), 484
- Moulton, Lord, *Heilbut, Symons* case (1913), 249
- Mummery LJ
 - Anglo Petroleum Ltd v. TFB (Mortgages) Ltd* (2007) 7, 640
 - Horsfall v. Haywards* (1999), 574
 - Pesticcion v. Huet* (2004), 328
- Mustill Lord, 508
 - arbitration, 668
 - Charter Reinsurance Co. Ltd v. Fagan* (1997), 392, 393, 495, 496
 - FC Shepherd v. Jerrom* (1987), 448, 461
 - 'The Golden Victory'* (2007), 573
 - Hussey v. Eels* (1990), 580
 - Lombard North Central plc v. Butterworth* (1987), 499
 - Malcolm v. Chancellor, Masters & Scholars of the University of Oxford* (1994), 96
 - Ruxley Electronics Ltd v. Forsyth* (1996), 548

- negligence, 253, 355, 374–5, 553–4
 - contributory negligence, 23, 260, 556, 582–6
 - availability of, 585
 - reform of the law on, 584–5
 - in the ‘soft law’ codes, 657
 - and uncertainty, 585
 - economic loss resulting from, 128
 - and exclusion clauses, 429, 434
 - professional negligence, 571
 - reasonable foreseeability, 558
- Neill, Lord, 27–8
- Neill, Sir Brian, *Stocznia Gdynia SA v. Gearbulk Holdings Ltd* (2009), 480
- Neill LJ, *Thake v. Maurice* (1986), 87
- Nelson J
 - Thames Trains Ltd v. Adams* (2006), 85
 - Weldon v. GRE Linked Life Assurance Ltd* (2000), 366
- Neuberger, Lord
 - Kinch v. Ballard* (1999), 56
 - Kyle Bay Ltd v. Underwriters etc.* (2007), 283
 - Liverpool CC v. Walton* (2002), 92
 - Tennaro case* (2003), 615
 - Thorner v. Major* (2009), 385
- Nicholas, Lord, *Royal Bank of Scotland v. Etridge (No. 2)* (2002), 326
- Nicholls, Lord
 - Attorney-General v. Blake* (2001), 589–90, 592
 - Gran Gelato Ltd v. Richliff Ltd* (1992), 257
 - Grant v. Bragg* (2009), 259
 - Jobson case* (1989), 607
 - Royal Bank of Scotland v. Etridge (No. 2)* (2002), 324, 327
 - Sempra Metals Ltd v. Inland Revenue Commissioners* (2007), 597
 - Shogun Finance Co. Ltd v. Hudson* (2003), 300
 - Thompson v. Foy* (2009), 321
- Nolan, Donal, 46
- Nolan LJ, *Schering Agrochemicals Ltd v. Resibel NVSA* (1992), 577
- Nourse LJ
 - Alpenstow Ltd v. Regalian Properties Ltd* (1985), 174
 - Barclays Bank plc v. Fairclough Building* (1995), 583
 - Hammond v. Osborn* (2002), 324
 - Thake v. Maurice* (1986), 87
 - Warren v. Mendy* (1989), 539
- objective principle, 7, 39, 275, 302
 - exceptions to, 294
 - and interpretation and rectification of written contracts, 382, 386
 - and offer and acceptance, 78
 - awareness of the object of the offer, 80
 - and mental incapacity, 79
 - rationale for, 78
 - and ‘reasonableness’, 86
 - unilateral errors, 86, 275
- Occam’s Razor, 566, 571
- offer and acceptance, 8, 37–87
 - posting before discovering attempted revocation, 52
 - acceptance in unilateral contracts, 66–70
 - time of acceptance, 69
 - auctions, tenders and fixed bid competition, 70
 - auctions, 70
 - ‘implied collateral’ obligation, 71
 - sealed bids, 75
 - tenders, 71
 - battle of the forms, 59–63
 - amalgamation of competing terms, 59
 - both sets of shots, 61
 - declaration of no contract, 59
 - ‘first shot’ theory, 61
 - implied terms, 59
 - ‘last shot’ theory, 59, 60, 61, 62
 - reasonable implication, 61
 - in the ‘soft law’ codes, 654
 - cancellation of the offer, 38
 - counter-offers, 37, 57–9
 - re-affirmation of the original offer, 58
 - rejection of the counter-offer, 58
 - course of dealing between the parties, 49
 - and the intent to create legal relations, 172, 184
 - and invitations to treat, 37, 39–41
 - advertisements, 40–1
 - goods on display, 41
 - and the objective principle, 39, 78
 - acquiescence in another’s belief, 84
 - awareness of mistake as to quality, value or nature of subject matter, 82
 - awareness of mistaken presentation of terms, 80
 - awareness of mistaken presentation or acceptance, 81
 - awareness of the object of the offer, 80
 - and mental incapacity, 79
 - misleading presentation or acceptance of terms, 80
 - rationale for, 78
 - and ‘reasonableness’, 86
 - situations where a valid contract exists, 79

- situations where there is no consensus, 79
- unilateral errors, 82, 86
- particular contexts, 38
 - reserve prices, 38
 - sealed bids, 38
 - tenders, 38
- postal acceptances, 50–7
 - acceptor's second thoughts, 56–7
 - appropriateness of postal acceptance, 53–6
 - delayed postal acceptance, 52–3
 - e-mail, 51
 - lost postal acceptance, 53
 - 'manifest inconvenience and absurdity', 55–6
 - place of formation, 52
 - posted rejection overtaken by acceptance, 57
- postal rule, 38, 50–1, 54, 57
- process of, 42–50
 - acceptance and the problem of silence, 47–9
 - conduct by offeree, 49–50
 - 'cooling off' periods, 47
 - cross-offers, 44
 - need for awareness of offer, 44
 - notification of acceptance, 44–5
 - postal acceptance, 45
 - problem of equivocality, 47–8
 - timing of acceptance (other than by post), 45–7
- revocation and termination of offers, 63–5
 - communicated rejection of offer, 65
 - direct or indirect revocation of firm offers, 63–5
 - lapse of time, 65
 - reform of the firm offer rule, 64–5, 653
- revocation of acceptance, 38
- silence as consent, 47–9
 - qualifications, 49–50
 - silence by the party initiating a proposal, 49
- tenders
 - at common law, 72
 - good faith in the process, 73
 - obligations upon the invitor, 72
- and unilateral contracts, 39
- Oliver J, *Radford v. De Froberville* (1977), 545, 546
- Ormrod LJ
 - 'The Hansa Nord' (1976), 505
 - Snelling v. John Snelling Ltd* (1973), 205, 596
- Orr LJ, *H Parsons (Livestock) Ltd v. Uttley Ingham & Co. Ltd* (1978), 562, 563, 570
- O'Sullivan, Janet, 147
- Otton LJ, *Duffen v. FRA BO SpA*, (1998), 607
- Parke B, *Robinson v. Harman* (1848), 540
- Parker LJ, Jonathan, *Conlon v. Simms* (2006) 4, 272
- parol evidence rule, 251–2, 299, 384
 - critique of, 406–7
 - and interpretation of written contracts, 405–7
 - qualifications upon, 405–6
 - reasons for supporting, 405
 - and rectification, 411
- Patten LJ
 - Durham Tees Valley Airport Ltd v. bmibaby Ltd* (2010), 93, 94, 543
 - Rainy Sky* case (2010), 391
- Pearce LJ
 - Archbolds (Freightage) Ltd v. S Spanglett Ltd* (1961), 639
 - C Czarnikow Ltd v. Koufos ('The Heron II')* (1969), 561
- PECL, *Principles of European Contract Law*, 4, 59–60, 396, 397, 511, 649, 650, 671
 - Article 2:101 (1), 654
 - Article 2:301, 653
 - Article 5:101, interpretation, 656
 - Article 5:102, relevant circumstances, 656
 - Article 9:102, specific performance, 657
 - Article 9:503, foreseeability, 658
 - assurance of performance, 487
 - contributory negligence, 584
 - damages, 611
 - frustration, 457–8
 - good faith, 20, 653
 - interpretation, 656
- Peden, Elizabeth, 356
- Peel, Edwin, 237, 573
- penalty doctrine, 599, 601–3
 - acceleration clauses, 608
 - breach triggering liability, 603–4
 - commercial parties, 605–6
 - consequence of finding a penalty, 608–9
 - in the context of money obligations, 607–8
 - critique of, 610–11
 - inequality of bargaining power, 606
 - invalid liquidated damages clause not a cap, 609–10
 - and liquidated damages, 601–11
 - need for breach as between payor and payee, 604–5
 - 'no deterrent purpose' test, 606–7
 - penalty in the context of money obligations, 607–8
 - rejoinder to the critique, 611
 - single sum payable, 607
 - statement of the doctrine, 601–3
 - time of assessment, 603

- penalty doctrine (*cont.*)
 - types of clauses covered by, 605
 - valid liquidated damages clause acts as a cap, 609
- performance, 475–515; *see also* specific
 - performance
 - and acceptance, 66
 - and good faith, 661
 - part-performance, 92
 - right to refuse, 477
 - right to withhold, 482
 - in the 'soft law' codes, 656
 - vicarious performance, 226
- Phillips, Lord
 - Campbell v. Frisbee* (2002), 511
 - Great Peace Shipping Ltd v. Tsavlis Salvage (International) Ltd* (2002), 282, 289, 377, 451
 - Lemenda Trading Co. Ltd v. African Middle East Petroleum Co. Ltd* (1988), 635
 - The Office of Fair Trading v. Abbey National plc* (2009), 439
 - Stone & Rolls* case (2009), 1391, 626
- Pill LJ, *Gardner v. Marsh & Parsons (a firm)* (1997) 621
- Pollock, Sir Frederick, 125, 139
- Porter, Lord, *Heyman v. Darwins Ltd* (1942), 484–5, 486
- postal rule, 38, 50–1, 54, 57
- Potter LJ, *Phillips v. Enron* (1997), 28, 91–2
- pre-contractual phase of contract formation, 19–35
 - abortive negotiations, 19–20
 - proprietary estoppel, 23
 - unjust enrichment or restitutionary relief, 21–3
- agreement to negotiate main contract in good faith, 25–6
- agreements ancillary to a settled agreement, 30–4
 - agreement to use reasonable endeavours to obtain official permission, 30–1
 - post-formation negotiation agreements, 31–3
 - post-formation obligation to observe 'utmost good faith', 33–4
- good faith in, 661, 663
- mediation agreements, 34–5
 - clauses requiring 'expert determination', 35
- negotiation agreements prior to formation of the main contract, 23–30, 386
 - agreement to negotiate in good faith, 24
 - agreement to use best endeavours to reach agreement, 27–8
 - ancillary obligations, 24
 - exclusivity agreements, 24
 - good faith, 24
 - obligation to reach agreement, 24
- predictability, 79, 317, 664
- private law, 650
- privity of contract, 9, 188, 189, 190–4, 217–18, 221–3
 - and collateral warranties, 292
- procedural unfairness, 339
- professional relationships, 10, 209, 239
- promises, 7, 131, 175
 - apparent promises, 171, 179, 180
 - classification of promissory terms, 490
 - gratuitous promises, 119, 121, 125, 147, 183
 - unenforceability of, 163
 - joint promisees, 188, 194–5
 - negative promises, 537
 - reasons for enforcing, 120–1
 - between spouses, 176
 - trusts of promises, 188, 193, 196, 197–8
- property rights, 190, 588
- public policy, 453–4, 621–45
 - agreements involving a restraint of trade, 637–8
 - agreements to deceive or cheat public authorities, 635
 - agreements to oust the court's jurisdiction, 636–7
 - contracting involving or intending to promote sexual immorality, 630–1
 - contracts affecting foreign policy, 634
 - contracts tending to pervert the course of justice, 635–6
 - contracts tending towards corruption in public office, 635
 - servitude, 633–4
 - unacceptable agreements concerning matrimony, 631–3
- Purchas LJ
 - Schering Agrochemicals Ltd v. Resibel NVSA* (1992), 577
 - Williams v. Roffey & Nicholls (Contractors)* (1991), 143, 144
- Radcliffe, Lord, 668
 - Bridge v. Campbell Discount* (1962), 606
 - Davis Contractors Ltd v. Fareham UDC* (1956), 377, 445, 447–8, 449–50, 456
- reasonable expectations, 367, 377, 670
- reasonableness, 369, 371, 372, 389–90, 429, 430, 664
 - and the Unfair Contract Terms Act 1977, 431–3
- rectification, 405, 407–17
 - and acquiescence, 417
 - and arbitration, 417

- Chartbrook Ltd v. Persimmon Homes Ltd* (2009), 414–15
- common intention error, 409–10
- discretionary form of relief, 408
- elements of, 409
- and error of law, 412
- estoppel by convention, 409
- and extrinsic evidence, 408, 413
- in favour of a mistaken party, 413–14
- and formal transactions, 413
- and good faith, 416
- high standard of proof, 412
- and implied terms, 409
- main propositions, 407–9
- and mistake, 408
- parol evidence rule, 413
- scope for, 408
- settled formula is decisive, 410
- settled understanding but botched formula, 410–12
- third party rights, 416–17
- and unilateral error, 413–14, 415–16
- the user principle, 592–5
- Reid, Lord
- A Schroeder Music Publishing Co. Ltd v. Macaulay* (1974), 638
- C Czarnikow Ltd v. Koufos* ('The Heron II') (1969), 561, 562
- 'The Heron II' (1969), 556
- 'legitimate interest' test, 527
- McCutcheon v. David MacBrayne Ltd* (1964), 7, 78
- Schuler (L) AG v. Wickman Machine Tool Sales Ltd* (1974), 495
- White & Carter v. McGregor* (1962), 375–6, 525, 526, 529
- Whitworth Street Estates (Manchester) Ltd v. James Miller & Partners Ltd* (1970), 387
- reliance, 158, 213, 242, 244–8, 544
- induced reliance, 120, 163
- reliance loss, 210, 540–1, 600, 604, 605
- remoteness, 542, 556, 557, 559–68, 569–70, 657–9
- case law, 568–70
- and scope of duty tests, 566–8
- in the 'soft law' codes, 657, 658, 659
- Research Group on EC Private Law (Acquis Group), 650
- restitution, 11–12, 22, 520–1, 586–95, 643–5
- account of profits, 592, 593
- based on unjust enrichment, 586
- Civil Law Reform Bill (draft), 596
- equitable account, 586
- forms of, 12, 587–8
- compensation for loss of opportunity to grant release of rights, 591
- disgorgement of gains made in breach of contract, 12, 588–91
- money recovered for total failure of consideration, 12, 586–7
- recovery in respect of goods or services, 12
- and frustration, 587
- obligation to pay the reasonable market value, 19
- quantum meruit*, 588, 641
- reduction of the amount for slow performance, 23
- remedies available, 11
- equitable account, 11
- sufficient, 158
- the user principle, 591
- restraint of trade, 340, 637–8
- Reynolds, F. M. B., 573
- Rix LJ
- Avon Insurance plc v. Swire Fraser Ltd* (2000), 241, 257
- Mamidoil-Jetoil Greek Petroleum Co. Ltd v. Okta Crude Oil Refinery (No. 1)* (2001), 103–4
- Offer-Hoar v. Larkstore Ltd* (2006), 230
- 'The Sea Angel' (2007), 451–2, 454
- Stocznia Gdynia SA v. Gearbulk Holdings Ltd* (2002), 509
- Rodger, Lord
- Chartbrook Ltd v. Persimmon Homes Ltd* (2009), 395
- Transfield Shipping Inc. v. Mercator* ('The Achilleas') (2008), 562, 564–5
- Romer LJ, *With v. O'Flanagan* (1936), 242, 244
- Roskill, Lord
- ASLEF* case (1972), 359
- Bunge Corporation v. Tradax Export SA* (1981), 492
- Export Credits Guarantee Department* (1983), 604–5
- 'The Hansa Nord' (1976), 505
- 'The Nema' (1982), 459
- Rowan, S., 533, 538, 545, 589
- Russell, LJ
- Taylor v. Bhail* (1996), 642
- Williams v. Roffey & Nicholls (Contractors)* (1991), 143–4
- Russell, Lord
- Luxor (Eastbourne) Ltd v. Cooper* (1941), 70
- Sachs LJ
- Bolton v. Mahadeva* (1972), 515
- Lloyd's Bank v. Bundy* (1975), 323, 330

- Sales J, *BMS Computer Solutions Inc. v. AB Agri Ltd* (2010), 472
- Salmon, Lord
Hongkong Fir case (1962), 500
Jones v. Padavatton (1969), 178
Liverpool City Council v. Irwin (1977), 357
- Sankey J, *Horwood v. Millar's Timber and Trading Co. Ltd* (1916), 634
- Sargant J, *Balfour v. Balfour* (1919), 176
- Saville LJ
Alfred Toepfer International GmbH v. Itegrani Export SA (1993), 487
Hughes v. Asset Managers plc (1995), 628
- Scarman, Lord
H Parsons (Livestock) Ltd v. Uttley Ingham & Co. Ltd (1978), 562, 563, 570
National Westminster Bank plc v. Morgan (1985), 325, 341
Tai Hing Ltd v. Liu Chong Hing Bank (1979), 375
'The Universe Sentinel' (1983), 311, 312
Woodar rule, 489
- Scott, Lord
BCCI v. Ali (2000), 86
Cobbe v. Yeoman's Row Management Ltd (2008), 163, 164, 165
Equitable Life Assurance Co. Ltd v. Hyman (2002), 368
Farley v. Skinner (2001), 552
R v. Her Majesty's Attorney-General for England and Wales (2003), 330
Schering Agrochemicals Ltd v. Resibel NVSA (1992), 577
- Scottish Law Commission, 667
- Scrutton LJ
Foley v. Classique Coaches (1934), 102
Lens v. Devonshire Club (1914), 179
Re Mahmoud and Ispahani (1921), 643
Re Moore & Co. and Landauer & Co. (1921), 503
Reigate v. Union Manufacturing Co. (Ramsbottom) Ltd (1918), 364, 365
- Sedley LJ, *Brennan v. Bolt Burdon* (2003) 283
- Selborne, Lord, *Scarf v. Jardine* (1882), 231
- Shaw LJ, *Howard Marine and Dredging Co. Ltd v. A. Ogden & Sons (Excavations) Ltd* (1978), 258
- Simon, Lord
Barton v. Armstrong (1976), 315
BP Refinery (Westernport) Pty Ltd v. Shire of Hastings, 365
British Movietone News Ltd v. London District Cinemas (1952), 456
'The Dynamic' (2003), 526, 528
- HHR Pascal BV v. W2005 Puppert II BV* (2009), 390
- National Carriers Ltd v. Panalpina (Northern) Ltd* (1981), 451
- New Zealand Shipping v. Satterthwaite ('The Eurymedon')* (1975) C, 219
- Rainy Sky* case (2010), 391
- Simpson, Brian, 590
- Singleton J, *Hartog v. Colin & Shields* (1939), 81
- Slade LJ
Agip SpA v. Navigazione Alta Italia SpA ('The Nai Genova') (1984), 413
BCCI v. Aboody (1990), 321
- Smith, Prof. Sir John, 285–6
- Smith LJ
Maggs v. Marsh (2006), 387
Maple Leaf Macro Volatility Master Fund v. Rouvroy (2009), 42–3, 78
Office of Fair Trading v. Abbey National plc (2009), 604
Pitts v. Jones (2007), 130
- 'soft law' contract law codes, 4, 59–60, 649–72
- acceptance rules, 653–4
 - battle of the forms, 654
 - codification, 665–72
 - consequences of breach of contract, 659
 - consideration, 654
 - contributory negligence, 657
 - damages, 657
 - and English contract law, 652–9
 - firm offer rule, 653
 - good faith, 653
 - interpretation of written contracts, 396
 - mistake, 292, 655
 - performance, 656
 - remoteness of damage, 657–9
 - specific performance, 657
 - supervening difficulty, 655
- Somervell LJ
Errington v. Errington & Woods (1952), 69
Stockloser v. Johnson (1954), 612
- specific performance, 12, 112–13, 198–9, 210, 520, 530–7
- for breach of contract, 520
 - denial of in frustration, 473
 - limits on, 520
 - and mistake, 275, 293–4
 - in the 'soft law' codes, 657
- Spencer, John, 423
- Staughton LJ
Assicurazioni Generali SpA v. Arab Insurance Group (BSC) (2002), 246–7

- New Hampshire Insurance Co. v. MGN Ltd* (1995), 392
- Ruxley Electronics Ltd v. Forsyth* (1996), 547
- '*The Solholt*' (1983), 576
- Steinfeld QC, *Alan, Aribisala case* (2007), 614–15
- Stephenson LJ, *Alan v. El Nasr* (1972), 153
- Stevens, R., 84, 406
- Steyn, Lord, 92
- CTN Cash & Carry Ltd v. Gallaher* (1994), 313, 341
- Director General of Fair Trading v. First National Bank plc* (2002), 439, 662
- Equitable Life Assurance Co. Ltd v. Hyman* (2002), 356, 367, 368
- First Energy (UK) Ltd v. Hungarian International Bank Ltd* (1993), 664
- Manual Investment Co. v. Eagle Star Life Assurance* (1997), 388, 390
- Smith New Court case* (1997), 255, 257–8
- Trentham (Percy) Ltd v. Archital Luxfer* (1993), 42
- Vitol SA v. Norelf Ltd ('The Santa Clara')* (1996), 47, 509–10
- Stocker LJ, *Quadrant Visual Communications Pty Ltd v. Hutchison Telephone (UK) Ltd* (1993), 533
- Strauss QC, Nicholas, 525
- Ministry of Sound (Ireland) v. World Online Ltd* (2003), 528
- Stuart-Smith LJ
- Allied Maples Group v. Simmons & Simmons* (1995) 550
- Commission for New Towns v. Cooper (GB) Ltd* (1995) A, 415–16
- Study Group on a European Civil Code, 650
- Sumner, Lord, *Hirji Mulji v. Cheong Yue Steamship Co. Ltd* (1926), 446
- Swift J
- Silverman v. Imperial London Hotels* (1927), 363
- Tan, D. S., 318
- Teare J, *Sheffield United Football Club Ltd v. West Ham United Football Club plc* (2008), 351
- Templeman, Lord
- Boustany v. Piggott* (1995), 336
- Harvela v. Royal Trust Co. of Canada* (1986), 77
- terms, 345–51; see also implied terms
- ancillary agreements or clauses, 347–51
 - agreements 'subject to contract', 347–8
 - arbitration clauses, 349–51
 - arbitration: finality clauses, 351
 - choice-of-law clauses, 348
 - collateral warranties, 347
 - entire agreement clauses, 347
 - and the European Jurisdiction zone, 349–51
 - exclusion clauses, 347
 - force majeure* clauses, 347
 - hybrid arbitration and jurisdiction clauses, 351
 - jurisdiction clauses, 348, 349–51
 - mediation agreements, 348
 - non-reliance clauses, 347
- classification of, 345–7
- express terms, 346–7
 - implied terms, 346–7
 - non-promissory terms, 346–7
 - promissory terms, 346–7
- Thankerton, Lord, *Hillas & Co. v. Arcos Ltd* (1932), 93
- Thesiger LJ, *Household Fire Insurance Co. v. Grant* (1879), 53
- third party rights, 187–223
- actions brought by the promisee, 198–206
 - building contracts, 200–6
 - damages, 199–200
 - debt, 198
 - specific performance, 198–9
 - the benefit of exclusion clauses, 217–21
 - and the carriage of goods, 217, 219–20
 - in common law, 187
- Contracts (Rights of Third Parties) Act 1999
- arbitration clauses, 215–16
 - clause permitting variable selection of third party, 213
 - common law rights of the promisee, 213–14
 - damages, 210
 - double compensation, 214–15
 - exclusion of the Act by contracting parties, 215
 - limitation of actions, 215
 - manifestation of assent, 212–13
 - 'master clause' in favour of A and B, 213
 - parallel third party rights of action, 214
 - right of defence or set-off, 210–11
 - specific performance, 210
 - third party's remedies, 209
 - variation or rescission of the contract, 211–12
- cost of cure, 202, 203, 204
- declarations, 205–6
- and the doctrine of privity, 190–4
- assessment of the doctrine, 192–4
 - and exclusion clauses, 194
- exclusion clauses, 217–21
- and the Contracts (Rights of Third Parties) Act 1999, 218

- third party rights (*cont.*)
 - Himalaya* clauses, 218–20
 - non-exclusive jurisdiction clauses, 220–1
- joint promisees, 188, 194–5
 - declaration of the trust, 195
 - effects, 195–6
 - joinder rule, 195
- no third party burden principle, 189
 - types of ‘burden’, 190
- privity of contract and ‘burden’, 221–3
 - bailment of goods ‘on terms’, 222
 - inducing a breach of contract, 221–2
 - injunction to prevent interference, 222
 - nature of bailment, 223
 - restrictive covenants affecting land, 222
 - unlawful interference with a contract, 221–2
- stay of proceedings, 205–6
- trusts of promises, 195–8
- Thomas LJ, *Sunrock Aircraft Corp v. Scandinavian Airlines Systems* (2007), 550
- Thorpe LJ, *Rainy Sky* case (2010), 391
- tort law
 - and contract law, 569–70
 - damages, 253, 552–4
 - deceit, 11, 246, 253–6, 553–4, 641
 - duty of care, 359, 554
 - inducing a breach of contract, 221–2
 - and misrepresentation, 253
 - negligence, 11, 127–9, 355, 374–5
 - reasonable foreseeability, 558
 - unlawful interference with a contract, 221–2
- Toulmin J, *Mirant Asia-Pacific Construction (Hong Kong) Ltd v. Ove Arup & Partners International Ltd* (2007), 203–4
- Toulson LJ
 - Durham Tees Valley Airport Ltd v. bmibaby Ltd* (2010), 93–4
 - Great Peace Shipping Ltd v. Tsavliris Salvage (International) Ltd* (2002), 286
 - IFE Fund SA v. Goldman Sachs* (2007), 240–1, 266–7
 - LJ Korbetis v. Transgrain Shipping BV* (2005), 52–3
 - scepticism toward the scope of duty test, 565–6
 - Supershold Ltd v. Siemens Building Technologies FE Ltd* (2010), 555, 556–7, 558, 562, 566–8, 571
- Treitel, G. H., 57, 63, 71, 213, 263, 410
 - BP Exploration Co. (Libya) Ltd v. Hunt (No. 2)* (1979), 470–1
 - draft Contract Code, 667
 - frustration, 456
 - ‘*The Golden Victory*’ (2007), 573
 - illegality, 627, 642–3
 - misrepresentation, 243
 - offer and acceptance, 41
 - parol evidence rule, 406
 - Sale of Goods Act 1979, 502, 503–4
- trust, relationships of, 273, 328, 329, 359
- trusts of promises, 188, 193
 - and arbitration clauses, 197–8
 - based on mercantile custom, 196
 - confined to money and property transfers, 197
 - and direct rights of action, 197–8
 - implied, 196
 - irrevocability, 197
 - requirement for all three parties to participate in litigation, 197
 - requirement of explicit creation, 197
 - requirements for the creation of, 196–7
- Tucker J
 - Atlas Express Ltd v. Kafco (Importers and Distributors) Ltd* (1989) 3, 319–20
- Turpin, Colin, 56
- uncertainty, 89, 341, 661, 664, 670
 - and contributory negligence, 585
- unconscionability, 307–8, 334–9
 - and coercion, 334
 - and ‘gross disparity’, 338
 - and undue influence, 337–9
- undue influence, 307, 321–34
 - and coercion, 325, 331–2
 - duty not to suppress a material factor, 329
 - elements of, 335–6
 - and misrepresentation, 331–2
 - nature of, 321–6
 - a positive duty to act, 330
 - presumed undue influence, 326
 - categories of, 326–8
 - and procedural unfairness, 339
 - and relationships of trust and confidence, 328, 329
 - banker and customer, 329–31
 - constructive notices, 333
 - independent advice for guarantors, 333
 - lenders, guarantors and third parties, 331–3
 - requirements for, 321
 - rescission for, 322
 - and unconscionability, 337–9
- Ungoed-Thomas J, *Cunliffe-Owen v. Teather & Greenwood* (1967), 373–4

- UNIDROIT *Principles of International Commercial Contracts*, 4, 59–60, 397, 511, 649, 650, 668, 671
- Article 4.3, interpretation, 656
- Article 7.2.2, specific performance, 657
- Article 7.4.4, foreseeability, 658
- Articles 1.3 and 3.2, 654
- assurance of performance, 487–8
- contractual modification, 148
- contributory negligence, 584
- damages, 611, 659
- duress, 314
- exclusion clauses, 422
- frustration, 458
- good faith, 653
- ‘gross disparity’, 338–9
- inconsistent behaviour, 121
- mistake, 292
- uniform law projects, 668
- unjust enrichment. *see* restitution
- Upjohn, Lord, *C Czarnikow Ltd v. Koufos* (‘*The Heron II*’) (1969), 562
- USA
- good faith, 660
- interpretation of written contracts, 397
- Lefkowitz v. Great Minneapolis Surplus Store* (1957), 40
- Restatement on Contracts*, 660, 670
- Uniform Commercial Code, 487, 660, 670
- Valcke, Catherine, 398
- Vaughan-Williams LJ, *Krell v. Henry* (1903), 461
- Vienna Convention on Contracts for the International Sale of Goods, 651, 657, 658
- Vogenauer, Stefan, 650
- Vos J, ‘Chelsea Barracks case’, 30, 33–4
- Waddams, S., 660
- Walker, Lord
- Cobbe v. Yeoman’s Row Management Ltd* (2008), 160, 163, 165
- Jackson v. Royal Bank of Scotland* (2005), 557, 569
- Shogun Finance Co. Ltd v. Hudson* (2003), 300, 302, 303, 304
- Transfield Shipping Inc. v. Mercator* (‘*The Achilles*’) (2008), 564, 566, 567, 571
- Waller LJ
- Avraamides v. Colwill* (2006), 207
- Equitable Life Assurance Co. Ltd v. Hyman* (2002), 368
- Mulvenna v. Royal Bank of Scotland plc* (2003), 569
- ‘*The Seaflower*’ (2001), 491
- Whittle Movers Ltd v. Hollywood Express Ltd* (2009), 109–10
- Ward LJ
- Drew v. Daniel* (2005) 323
- Hammond v. Osborn* (2002), 324
- warranties, 7, 248–52, 267, 405
- Warrington, Lord
- Balfour v. Balfour* (1919) A, 175, 176
- May & Butcher v. R* (1934), 101
- Wednesbury principles, 369
- Whittaker, S., 498
- Widgery LJ, *Merritt v. Merritt* (1970), 177
- Wigram V-C, 196
- Henderson v. Henderson* (1843), 593
- Wilberforce, Lord
- Barton v. Armstrong* (1976) C, 315
- Brinkibon v. Stahag Stahl* (1983), 46
- Bunge Corporation v. Tradax Export SA* (1981), 492, 493
- Johnson v. Agnew* (1980), 263–4, 512
- National Carriers Ltd v. Panalpina (Northern) Ltd* (1981), 463
- New Zealand Shipping v. Satterthwaite* (‘*The Eurymedon*’) (1975), 42
- Photo Production Ltd v. Securicor Transport Ltd* (1980), 426
- Prenn v. Simmonds* (1971), 394–5
- Reardon Smith Line case*, (1976), 388
- Schuler (L) AG v. Wickman Machine Tool Sales Ltd* (1974), 493, 496, 500
- Winn LJ, *D & C Builders v. Rees* (1966), 150, 157
- Wood V-C, *Barry v. Croskey* (1861), 241
- Woodar rule, 199–200, 489
- exceptions to, 199, 200, 203
- Woolf, Lord
- Equitable Life Assurance Co. Ltd v. Hyman* (2002) L, 368
- Philips Hong Kong case* (1993), 605–6
- Vaswani case* (1996), 489
- Wadham Stringer Finance Ltd v. Meany* (1981), 608
- Wright, Lord
- Luxor (Eastbourne) Ltd v. Cooper* (1941), 353, 358, 361, 365, 367, 369
- Maritime National Fish Ltd v. Ocean Trawlers Ltd* (1935), 452–3
- With v. O’Flanagan* (1936), 243
- written contracts
- assessment of the Investors Compensation Scheme Principles, 391–4

- written contracts (*cont.*)
 - bar on considering pre-contractual negotiations, 394–401
 - in jurisdictions other than Britain, 396
 - ‘private dictionary’ exception, 398–401
 - reasons for, 395–6
 - in a ‘commercial’ way, with sensitivity to
 - business ‘common sense’, 388
 - consideration of background, 389
 - consideration of business common sense, 390
 - consideration of the ‘commercial purpose’,
 - background, ‘context’, and its location in the relevant ‘market’, 388
 - contextual approach to interpretation, 388–9
 - exclusion of previous negotiations, 389
 - High Court decisions on, 384
 - interpretation and implied terms, 407
 - interpretation and rectification, 379–417
 - interpretation to eliminate errors, 401–4
 - Chartbrook Ltd v. Persimmon Homes Ltd* (2009), 403–4
 - reconstitutive interpretation, 401, 402–4
 - natural and ordinary meaning of words, 390
 - and the parol evidence rule, 405–7
 - and questions of law, 383–5
 - reasonableness, 389–90
 - rules governing interpretation, 385–94
 - and subsequent conduct of the parties, 387–8
- Yeo, T. M., 289
- Zander, Michael, 519